Clean Trade in Natural Resources

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The "resource curse" can strike countries that derive a large portion of their national income from exporting high-value natural resources, such as oil, gas, metals, and gems. Resource-exporting countries are subject to four overlapping curses: they are more prone to authoritarianism, they tend to suffer more corruption, they are at a higher risk for civil wars, and they exhibit greater economic instability.[1]

The correlations between resources and such pathologies as authoritarianism, corruption, civil conflict, and economic dysfunction are evident in the list of the five major African oil exporters: Algeria, Angola, Libya, Nigeria, and Sudan. The recent histories of mineral exporters support the correlations: for example, "blood diamonds" fueled Sierra Leone's decade-long civil war, and the continuing conflict in the metal-rich eastern Congo has caused up to 6 million deaths. The phenomenon is not solely African: Burma, Yemen, and Turkmenistan, for example, are also resource cursed. Moreover, poor governance in resource-cursed countries can engender follow-on pathologies, such as a propensity to cause environmental damage both domestically (for example, through the destruction of forests) and globally (through increased greenhouse gas emissions).

Most research on the resource curse has focused on the institutions of exporting countries. This essay focuses instead on importing countries, especially those in North America and Europe. I survey how the resource curse impedes core interests of importing states. I then discuss how the policies of importing states drive the resource curse, and how these policies violate their existing international commitments. The second half of the paper describes a policy framework for importing states that can improve international trade in resources for both importers and exporters.

The Resource Curse Harms Importing States

Importing states that engage commercially with resource-cursed countries risk channeling funds to hostile, repressive, or failing regimes in ways that threaten their own national priorities. For example, some of the regimes most antagonistic to the West

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in the past forty years, including the Soviet Union, Iran, Iraq, and Libya, have been financed by Western oil and gas payments. Resentment of repressive regimes in the Middle East—both among elites and on "the street"—has fueled radicalization and anger at the Western states that support those regimes. Taking the United States (the largest resource importer) as an example, most of the countries on the U.S. "State Sponsors of Terrorism" list have been oil exporters; and groups that the United States considers threats to peace (such as al-Qaeda and Hezbollah) have used conflict diamonds to escape U.S. asset freezes. Today terrorists continue to seek havens in areas of resource-fueled conflicts, such as the Great Lakes region of Africa.

One traditional importing-state strategy for securing resource access and supply has been to support "rentier" regimes, which sustain their rule by spending resource revenues on patronage and security forces. The long-term results of this strategy have been mixed. Regimes that do not respect the rule of law have tended to revise resource contracts unilaterally. Some rentier regimes have been overthrown by hostile forces (for example, the Shah in Iran) or have become hostile themselves (such as Gaddafi in Libya and Hussein in Iraq), resulting in restricted resource access for Western firms. Restricted access and political uncertainty have increased price volatility, which has contributed to global economic instability. (Four of the last five global recessions have been preceded by an oil price spike.) Moreover, even friendly rentier regimes tend to lose governance capacity over time, and regimes supported as strategic partners have found it harder to maintain order as their people gain greater access to information, adopt anti-state and anti-corporate ideologies, and acquire weapons (as in the Niger Delta and Yemen). The declining capacity of rentier regimes to govern has forced importing states and their extractive corporations to attempt remedial governance through foreign aid and through "corporate social responsibility" (for example, building schools and hospitals, monitoring environmental impacts). However, remedial governance is quite difficult, and opens states and firms that attempt it to escalating demands and protests from the local population.

Importing states and their resource companies face high risks when engaging with resource-cursed countries, yet the costs of withdrawal are also high. Unilateral commercial withdrawal from an exporting country cedes resource access to competitors, and is thus ineffective in reducing the resource curse. This combination of high risk in engagement and high cost of withdrawal creates strong strategic counterpressures on importing states. In this sense, importing states are themselves resource cursed.

Importing-state Policies Drive the Resource Curse

The resource curse threatens when state or nonstate actors gain control over foreign-origin resource revenues through violence or coercion, stealth or fraud, creating the potential for self-reinforcing cycles of revenue capture. Importing-state policies contribute to the resource curse by connecting the demand for resources to these unaccountable actors. Importing states are putting their citizens into business with authoritarians, armed groups, and corrupt officials abroad, driving the resource curse in exporting countries.

The key insight is that while there is an international market, there is no international system of property law. Each sovereign state controls its own system of private and public law. Each state thus decides which foreign persons have the legal right to sell goods into its jurisdiction. Specifically, each sovereign state determines which foreigners will have the legal right to sell foreign natural resources to its citizens and corporations, and therefore which foreigners will receive the money derived from its consumer demand in return. For example, at the time of this writing the U.S. government is granting Equatorial Guinea's authoritarian president Teodoro Obiang the legal right to sell his country's oil into American jurisdictions. Yet the United States has for several years denied the authoritarian president Omar al-Bashir the legal right to sell Sudan's oil to Americans (that is, the United States has maintained sanctions on the Sudanese regime). The United States has connected its consumer demand for oil to Obiang, but not to al-Bashir.

These decisions on commercial engagement with foreign actors are entirely discretionary for each sovereign state (except in cases of mandatory international sanctions). Every sovereign state decides for itself who has, and who lacks, the legal right to sell natural resources to its citizens and corporations. Moreover, the example of al-Bashir shows that the commercial decisions of importing states are separate from their decisions on the political recognition of other states. The United States has recognized Sudan as an independent state throughout the years it has denied President al-Bashir the legal right to sell Sudan's oil to Americans. Political recognition of a foreign state, and commercial engagement with any potential vendor of foreign resources, are entirely distinct decisions.

How do importing states decide which foreigners have the right to sell resources into their jurisdictions? The default policy of all importing states is to grant the legal right to sell natural resources to whoever can maintain coercive control over the territory where those resources are located. The standing policy of all importing states is "might makes right." Under this policy, importing states award the valuable prize of their consumer demand to whoever can control a country or region by any means, including through force or fear. This policy incentivizes authoritarianism and coups by promising substantial resource revenues to whichever actor can be most effectively coercive. When the standing policy is to reward whoever can be most ruthless, the most ruthless will rise toward the top.

The standing policy of “might makes right” also incentivizes the resource curse of civil conflict. It is not only those who gain control of a country’s government that are granted the legal right to sell resources; it is also those who gain control over some portion of a country’s territory. For example, before the U.S. Clean Diamonds Act of 2003, the blood diamonds sold by Sierra Leone’s brutal rebels were legally purchased in the United States. Today the seizure of a mineral deposit by armed groups in the eastern Congo anchors a chain of title that ends in the lawful sale of those minerals inside Germany, France, and Norway. When military capture of territory is rewarded with large revenue flows, one expects more, and better armed, militias.

Importing-state policies beyond “might makes right” also worsen the resource curse by encouraging corruption. Until 2006 the Netherlands allowed tax deductions on bribes to foreign officials; and it was not until 2009 that Britain successfully prosecuted a foreign corruption case. “Facilitation payments” are still permitted by Australia, Canada, New Zealand, South Korea, and the United States. Export credit agencies in many importing states fund and insure firms that pay off local officials. The world’s leading banks, hospitals, universities, and luxury shops legally provide goods and services in exchange for resource revenues taken fraudulently from national treasuries.

Commercial engagement with a resource-rich country is like plugging a high-voltage line into its political economy. If the country is well-wired politically and economically, it will glow brighter. If not, making the connection can cause short circuits, fires, and explosions. Importing states’ current policies lead them to make commercial connections everywhere: the default is to engage with whoever can control resources by whatever means. The incentives generated by these policies drive the resource curse.

Existing International Obligations Require Public Accountability Over Resources

Today’s standing trade policies of importing states are a remnant of the pre-modern (Westphalian) international system established in the seventeenth century. Pre-modern states endorsed the principle of “might makes right” in all areas of their foreign policy, and therefore affirmed as lawful the acquisition of territory by conquest, colonialism, minority rule, apartheid, and nearly unlimited violence by regimes against their own citizens. By contrast, the modern principles of international politics and law define a paradigm of international relations based on popular sovereignty and human rights.

These principles of the modern international order require public accountability over natural resources within each country. For example, 178 states (including all of the rich democracies) are parties to at least one of the two major human rights treaties: the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social, and Cultural Rights. These treaties have an identical Article 1, which declares, "All peoples may, for their own ends, freely dispose of their natural wealth and resources."

The fact that the great majority of states are parties to a major treaty requiring public accountability—including Sweden, India, Kuwait, Iran, South Korea, the United Kingdom, the United States, and Cambodia—shows that this requirement can be satisfied within quite different political and economic systems. Public accountability does not require a specific form of government, such as multiparty democracy. It is compatible with state ownership of natural resources, and with systems of law (such as in the United States) under which resources pass into private ownership. The principle of public accountability requires only that the citizens of a country, as the ultimate owners of the country's resources, can exercise some control over what is done with their resources—whether those resources will be conserved, nationalized, privatized, sold to foreigners, and so on. The less that citizens can control decisions over natural resources, the less legitimate those decisions are. At the limit, the property rights of a people are violated (as any owner's rights would be) when some actor gains control of their assets by force, threat, or extreme manipulation. Where the people lack any power to stop the sale of their assets, the sale of those assets is illegitimate. The transportation of resources out of that country is literally theft.

The importing states' default policy of "might makes right" undermines the property rights of the citizens of the worst resource-cursed countries by granting the legal authority to sell resources to actors whose decisions are entirely beyond the control of those citizens. This policy approves the theft of resources from exporting countries, and so breaches the property rules essential to any market order. Other importing-state policies, such as those that encourage corruption, also undermine the public accountability over resources that importing states have committed to support. With these policies, importing states are violating their commitments to primary principles of the modern international order.

A Clean Trade Policy Framework for Importing States

As Article 1 of the human rights covenants suggest, the idea of citizen sovereignty has become the modern world's touchstone for political legitimacy. Regardless of the actual political conditions in-country, the constitutions and politicians of nearly every state robustly affirm that the people have the ultimate right to rule their territory. The policy framework described below allows resource-importing states to align their policies with this primary norm of contemporary politics and law. The framework leverages the existing international agreement on principle to build a policy architecture on which importing states can converge.

For the sake of accountability to its own citizens, each importing state should publish its grounds for identifying who (including the current regime) is a legitimate vendor of the resources of countries from which it imports. Yet transparency alone is insufficient. Importing states should also reverse the policies that breach their international obligations and that drive the resource curse. Importing-state policies should stop the illegitimate trade with resource-exporting countries where public accountability is absent, and support public accountability in countries where it is weak.

The sharp end of a "Clean Trade" policy framework applies to countries where severe authoritarianism or state failure makes public accountability over resources impossible. Two Clean Trade policies, described below, are designed for these "worst of the worst" resource-cursed countries.

Disqualified Countries: A Clean Trade Act and Clean Hands Trusts

The ground rules of a free market require all participants to respect property rights. In countries where citizens lack the power to stop the sale of natural resources, the export of those assets is theft. The policy framework described here enables implementing states to block the direct importation of stolen resources, and to discourage the violation of property rules by other states.

An implementing state will declare countries with no public accountability over resources disqualified for resource exports. The political conditions in a disqualified country are so poor that its citizens could not possibly be exercising any check over the actors, selling off their assets, whether they are authoritarians or nonstate actors, such as rebels or warlords. Either the country's citizens cannot find out about the sale of the country's resources or they are too intimidated or vulnerable to protest these sales.

In concrete political terms, qualified and disqualified countries can be distinguished by whether citizens have minimal civil liberties and political rights. There must be at least some absolutely minimal press freedom if citizens are to have access to information about what is being done with their resources. If there is a functioning state, it must not be so thoroughly corrupt that it is impossible for the people to find out what is happening with the revenues from resource sales. Citizens must be able to pass information about resource sales to each other without fear of surveillance and arrest. The state must have some political mechanisms in place through which the people can effectively protest resource decisions: at least a nonelected consultative legislature that advises the regime, or at the very least the means by which civic groups can petition. There must be a minimally adequate rule of law, ensuring that citizens who wish to protest resource sales publicly and peacefully may do so without fear of cruel judicial punishment, disappearance, serious injury, or death.

An implementing state can define rule-based criteria for disqualification by reference to "worst of the worst" ratings on independent metrics. A variety of respected metrics already exist, including the World Bank Worldwide Governance Indicators, the Fund for Peace/*Foreign Policy* Failed States Index, the Transparency International Corruption Index, as well as those produced by Polity, Freedom House, the *Economist*, and so on.

At present, disqualified countries will likely be few, yet the potential for disqualification will exert upward pressure on public accountability in resource-exporting countries. For purposes of illustration, the lowest-ranked countries on the 2010 Fund for Peace/*Foreign Policy* failed state indices are Afghanistan, Burma, Chad, Equatorial Guinea, Guinea, North Korea, and Sudan. The 2010 Freedom House "worst of the worst" list is Burma, Equatorial Guinea, Eritrea, Libya, North Korea, Somalia, Sudan, Turkmenistan, and Uzbekistan.[2]

States implementing a Clean Trade framework will disengage their consumer demand from the most extreme authoritarian regimes and failed states, and encourage their trade partners to join them, with two policies: a Clean Trade Act and Clean Hands Trusts.

A Clean Trade Act

A Clean Trade Act will set out legal penalties for any citizen or corporation facilitating the import of natural resources from a disqualified country into the enacting jurisdiction. The legislation will also deny all commercial facilities of the enacting jurisdiction (financial, medical, educational, retail, and so on) to anyone in a disqualified country who sells natural resources out of that country. Implementing a Clean Trade Act will express no judgment on the political legitimacy of any foreign regime, as the distinction above between political recognition and commercial engagement shows. An implementing state can say that the political leadership of a foreign country is "none of our business," while saying that in current conditions its resource exporters qualify for "none of our business."

Passing a Clean Trade Act will create a level playing field for all corporations operating within the jurisdiction of the implementing state. The legislation will require all such firms not to do business in the worst resource-cursed countries, meaning that no firm will lose business to any other within the jurisdiction of the implementing state. A British Clean Trade Act, for example, will remove the competitive pressures between Shell and BP to sign contracts with the worst regimes.

Yet by itself a Clean Trade Act will disadvantage firms that are within the jurisdiction of the implementing state relative to those that are not. And by itself a Clean Trade Act will also disadvantage the implementing state relative to other states in the competition to secure natural resource flows. Recent U.S. sanctions on Sudan, for example, have mainly advantaged Asian national oil companies and Japan, and the money and arms that the Asian countries have given to al-Bashir in exchange for Sudan's oil have been more than sufficient to maintain al-Bashir in power in Khartoum. U.S. sanctions impose a commercial disadvantage on the United States and its firms, yet the resource curse in Sudan continues. States need new ways to exert horizontal pressure on other states to join them in commercially isolating countries where resources are controlled by unaccountable actors.

Clean Hands Trusts

Any state that passes a Clean Trade Act can exert this horizontal pressure on trade partners through the establishment of Clean Hands Trusts. These trusts are mechanisms to protect the citizens of the implementing state from paying for stolen resources indirectly, which will have the effect of penalizing trade partners for buying resources from extremely authoritarian or failed states. The trusts are underwritten by the principles of the modern international order, and enable states to advance their national interests by enforcing those principles. The operation of a Clean Hands Trust is described in the following scenario for a Clean Hands Trust for Equatorial Guinea:

Equatorial Guinea is a petroleum-rich country in Central Africa dominated since 1979 by its authoritarian president, Teodoro Obiang. Obiang's regime allows no significant political opposition, press freedom, or judicial independence. International observers have reported many cases of detention, torture, and extra-judicial killing of political opponents. Obiang's sales of Equatorial Guinea's petroleum are entirely beyond the control of the country's citizens, who have no means to "freely dispose of their natural wealth and resources." This means that Obiang's regime cannot be a legitimate vendor of the country's resources and cannot pass valid title to Equatorial Guinea's oil or gas.

Unilateral commercial detachment will not improve the situation in Equatorial Guinea. Were the United States, for example, to sanction Obiang's regime by passing a Clean Trade Act as described above, China's national oil companies would likely step in and the resource curse in Equatorial Guinea would continue. Moreover, as the Equatorial Guinean–Chinese sales went through, American consumers would continue to pay for stolen Equatorial Guinean oil because of America's trade with China. The Equatorial Guinean oil would percolate through the Chinese economy, and so become a factor in producing many of the goods exported from China to the United States. Even after the United States had blocked direct deals with Obiang's regime, American shoppers would still end up paying for Equatorial Guinea's stolen oil when buying Chinese-made clothing and electronics.

In this scenario, the U.S. government could fight the resource curse and enhance its strategic position by treating Obiang's shipments of oil to China as what they would be: the passing of stolen goods. Say, for example, that China buys $3 billion worth of oil from Obiang. The U.S. government's response should be to establish a Clean Hands Trust for Equatorial Guinea. This trust is a bank account that the U.S. government will fill until it contains $3 billion, the money coming from duties on Chinese imports as they enter the United States. The money in this trust will then be held for the citizens of Equatorial Guinea, the owners of the stolen assets, until a minimally accountable government is in place.

This Clean Hands Trust will protect the American people from becoming tainted with the oil that China buys illegally from Obiang. The duties will extract from Chinese imports the value of the oil taken from Equatorial Guinea, and the trust will hold this money until it can be returned to Equatorial Guinea's citizens. With the duties in place American consumers can buy Chinese imports with clean hands because the duties subtract from the price of those imports the value of the oil sold illegitimately by Obiang's regime. And with a trust in place the Chinese will have strong incentives not to buy more oil from Obiang: if China buys another $1 billion worth of oil, the United States will impose another $1 billion worth of duties on its goods. The Equatorial Guinean people, for their part, will know that there is a large sum of money waiting to be turned over to them if they can replace the regime that is stealing their assets. Further, all actors within and outside the country will know that the U.S. duties will be lifted once Obiang's regime is replaced by a legitimate vendor of the country's resources.

A Clean Hands Trust is horizontally transferable to other importing states. Any government that passes a Clean Trade Act may set up a Clean Hands Trust once the Chinese buy from Obiang. Each government that creates such a trust will then regularly update its public report of how much money its trust is holding. All governments must stop filling their trusts once the combined global total in all of the trusts equals the value of the Chinese contract ($3 billion). This gives the "clean" countries a competitive incentive to announce and fill their trusts as quickly as possible, while limiting the duties on the Chinese to the amount of the original property-rights violation.

The two Clean Trade policies are designed to be compatible with the rules of the World Trade Organization. Since this is a large topic I will instead take up a second kind of concern: that the policies amount to economic sanctions, which have had varied success in the past.

The two Clean Trade policies differ from traditional sanctions in two respects. First, they have a different justification, which is to enforce property rights in international markets and combat the resource curse. Second, the policies create a better alignment of incentives than traditional sanctions, and so are more likely to work. The weakness of traditional sanctions has been that exporters in the target country have sold resources to their patrons and to other repressive regimes. By contrast, Clean Hands Trusts create incentives for all states not to buy from the disqualified countries. Every state in a chain of title originating in a disqualified country (for example, China when it buys from Obiang, states that buy from oil traders that buy from Obiang, and so forth) will face trade penalties. Trade penalties here *track* the stolen natural resources, so any state handling these resources will automatically incur costs.

The Clean Trade policies will curtail the trade that fuels the resource curse. No commercially isolated regime can survive for long, and even the threat of commercial isolation may be sufficient to bring transformational pressures to bear. Moreover, once implemented, these policies will reduce the expected gains of potential authoritarians who might consider seizing control over resource revenues—through a coup or a civil war, for example.

Rules of Engagement and an Accountability Continuum

The Clean Trade Act and Clean Hands Trusts set policy toward the "worst of the worst" resource-cursed countries. Regarding the majority of resource-exporting countries, where there is some degree of public accountability over resources, states implementing the Clean Trade framework should effect a system of trade rules that sustains and encourages this accountability. To do so, implementing states can draw on any of the specific policies to combat the resource curse that are now available (regarding anticorruption, transparency, conflict prevention, and so on). Which policies to incorporate into the framework should be decided in specialized discussions in light of empirical research. This part of the framework is a structure for making existing policy options mutually reinforcing, by integrating these policies into a single trade architecture that supports public accountability in resource-exporting countries.

The policy framework is divided into two areas into which specific policies can be fit:

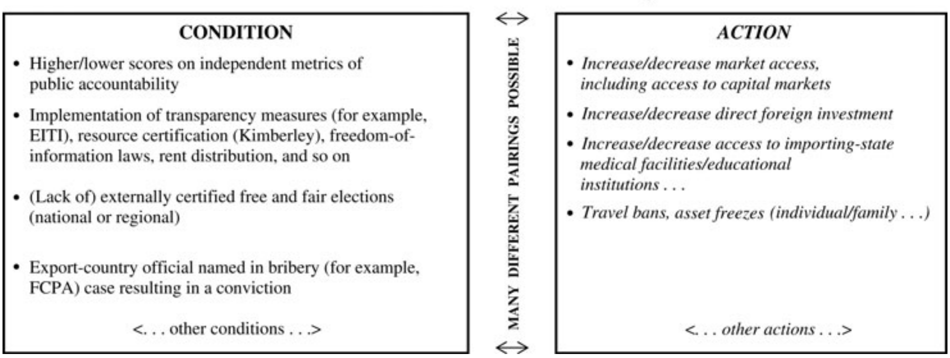
1. *Rules of Engagement for home actors dealing with resource exporters*. In this part of the framework importing states expand and enforce laws requiring persons within their own jurisdictions to do business with resource exporters in ways that strengthen public accountability in the exporting country. For example, states extend and enforce existing legislation regarding bribery, money laundering, corporate transparency, due diligence, and/or resource certification for imports (such as the Kimberley Process, which combats conflict minerals).
2. *An Accountability Continuum of commercial connections to exporting countries*. In this part of the framework importing states construct a rule-based system of conditionalities, offering more economic connections to those exporting countries that achieve greater public

accountability over resources. This system of conditionalities will be described in more detail.

For the past forty years major importers have structured their commercial engagement (concerning market access, export credits, and so on) around conditionalities. The compatibility of such conditionalities with the rules of the General Agreement on Tariffs and Trade is well understood. For example, the U.S. African Growth and Opportunity Act allows special trade privileges to sub-Saharan African countries with higher scores on rule-of-law, political pluralism, and anti-corruption indices. A Clean Trade policy framework sets out a continuum of increasing commercial connections to exporting countries contingent on the level of accountability over resources those countries attain.

Trade conditionalities match conditions in the exporting country to actions by the importing country. The lists below display a few of the options available for making commercial connections with exporting countries conditional on their public accountability. Many different conditionalities (that is, many different condition-action pairings) are possible.

Possible Conditionalities for an Accountability Continuum



The continuum of conditionalities should be constructed to offer more commercial connections to exporters achieving greater public accountability. Codifying an accountability continuum will allow states implementing the Clean Trade framework to make their terms of trade transparent and predictable. Implementing the framework will reverse the pressures in trade policy that today drive the resource curse.

Political Support for the Clean Trade Policy Framework

Any state may implement the Clean Trade policy framework unilaterally, in whole or in part, whenever it is politically feasible to do so. Implementation is within the authority of every sovereign state. All of the policies within such a framework are internal: they are all implemented within the state's jurisdiction so as to align the state's policies with its own principles. A state can commit to conditional implementation of the framework, leaving the choice of metrics (for example) to later multilateral agreement. A state can also commit to conditional enactment: for example, it can commit to enact the framework when states accounting for a certain percentage of global trade have also committed; or, for example, when a certain number of members of the European Union have also committed.

The framework will enjoy broad political support within implementing states. Friends of free markets will support the framework because its mechanisms strengthen the global market order by enforcing property rights. Protectionists will back the parts of the framework that insulate domestic industries from foreign competition. Those who prioritize national security will see measures that weaken hostile petrocrats, and that strengthen failed states where terrorism can incubate. Environmentalists will approve of reduced environmental damage from resource-cursed countries. Humanitarians will endorse the empowerment of some of the most mistreated people on earth. A Clean Trade policy framework will appeal across the political spectrum from right to left.

The resource curse forces importing states and resource corporations to pursue their legitimate interests from untenable positions, where their choices are either (1) to engage with and so empower odious, belligerent, and/or incompetent local actors, so becoming jointly responsible for their actions and failures; or (2) to withdraw, and thereby to cede resource access to competitors without changing the outcomes of the system. Feasible reforms that are grounded in settled international norms, and that will advance national interests, are available. The challenge is to push reform and to spread new rules horizontally through international cooperation. There are strong reasons for states to act together now—to enforce their own principles, and to lift their resource curse.

NOTES

[1] This article discusses the curses of authoritarianism, corruption, and civil conflict, leaving the economic phenomena mostly aside. For references to the literature relevant to this article, please see the background paper, available at wenar.info.

[2] All of these countries are significant resource exporters except Afghanistan, Eritrea, North Korea, and Somalia.