



SUDAN DIVESTMENT

TASK FORCE

A project of the Genocide Intervention Network

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**Response to Berkshire Hathaway's statement on its holdings in PetroChina Company Limited,
the majority-owned subsidiary of China National Petroleum Corporation (CNPC)
(February 21, 2007)**

Executive Summary

In late 2006, the Sudan Divestment Task Force, a project of the Genocide Intervention Network, asked major shareholders of PetroChina Company Limited (PetroChina) to engage the company regarding its connections to the ongoing genocide in the Darfur region of Sudan:

www.sudandivestment.org/docs/PetroChina_Request_to_Asset_Managers.pdf

In response to the combination of this request and inquiries from media and shareholders, Berkshire Hathaway, the largest holder of PetroChina stock in the US, released a statement on its PetroChina holdings on February 21, 2007 (www.berkshirehathaway.com/sudan.pdf). While the Sudan Divestment Task Force appreciates Berkshire Hathaway's willingness to comment on the company's holdings in PetroChina, we seek to clarify certain inaccuracies in the company's statement. This document briefly summarizes the detrimental role of PetroChina's parent company, China National Petroleum Corporation (CNPC), in Sudan's Darfur genocide and then traces the intimate, opaque, and symbiotic relationship between PetroChina and CNPC. The document then clarifies the most likely outcome in Sudan if shareholders ratcheted up pressure on PetroChina. Finally, the document lays out the Sudan Divestment Task Force's specific request of Berkshire Hathaway, namely one of shareholder engagement with PetroChina. It is our unwavering belief, supported by our extensive consultations with foreign policy experts, former government officials, and international organizations involved in Sudan, that vigorous and sustained shareholder engagement by Berkshire Hathaway with PetroChina would be a critical component of the international community's efforts to halt Darfur's slaughter.

The Darfur Genocide and China National Petroleum Corporation

The new millennium's first genocide rages unabated into its fourth year in the Darfur region of Sudan. For the first time in history, the U.S. government, along with numerous other political and non-profit entities, has declared that an *ongoing* massacre amounts to genocide. While an unprecedented grass-roots movement across the US and Europe has compelled governments and international organizations to take action, a few corporate actors in Sudan, including one of China's state-owned oil firms, China National Petroleum Corporation (CNPC), are actively exacerbating the crisis and frustrating these international efforts. CNPC's operations in Sudan, which represent nearly all of China's multi-billion dollar oil interests in the country, are problematic for multiple reasons (For further details, please see the Sudan Divestment Task Force's original report on "PetroChina, CNPC, and the Darfur Genocide" at http://www.sudandivestment.org/docs/PetroChina_Request_to_Asset_Managers.pdf):

- Because 70-80% of the income generated from Sudan's lucrative revenue sharing agreement with CNPC is funneled into its military, CNPC's operations in Sudan are an undeniable and well-documented enabler of Khartoum's genocidal policy in Darfur.
- CNPC's operations have also paved the way for a rampant arms trade between China and Sudan. As noted by the Washington Times in 2006, "In exchange for oil, Beijing provides weapons and diplomatic support [to Sudan]. China has supplied Sudan with tanks, artillery, helicopters and fighter aircraft. China has flooded Darfur with antipersonnel mines... Beijing has also helped Sudan build its own factories to manufacture small arms and ammunition, the real weapons of mass destruction in Khartoum's campaign of ethnic cleansing."
- Numerous reports have documented CNPC's willingness to house Sudanese military helicopters used in attacks on civilians at company airstrips. Furthermore, in the past, Beijing has explicitly asked Khartoum to send troops to places where CNPC operates, adding fuel to the accusations among human rights groups that CNPC helps facilitate displacement of local populations off of land where it intends to drill. Additionally, instead of employing Sudanese civilians, CNPC imports the majority of its labor from China.

The Intimate Affiliation Between PetroChina and CNPC

"To begin with, we have seen no records, including the various materials we have received from pro-divestment groups, that indicate PetroChina has operations in Sudan."

-- Berkshire Hathaway; Commentary on PetroChina holdings; February 21, 2007

Berkshire Hathaway is the largest US shareholder of CNPC's majority-owned subsidiary, PetroChina Company Limited (PetroChina). Importantly, shareholder investments in PetroChina are linked to CNPC through a unique, elaborate, and often opaque relationship between the two companies. This connection stands in stark contrast to the typical Western parent company-subsidary relationship. In its 2005 report justifying Harvard University's decision to divest its holdings in PetroChina, the Harvard Corporation addressed these exceptional links. Their findings, together with the Sudan Divestment Task Force's research, include the following:

Fluid Asset Transfers Between PetroChina and CNPC

- When CNPC planned its Initial Public Offering (IPO) on the New York Stock Exchange in early 2000, Western investor concerns about its operations in Sudan forced the company to scrap its initial IPO plans and instead carve out and offer a subsidiary, PetroChina, to the public which CNPC pledged would not be involved in Sudan activities.
- However, when PetroChina was offered to the public, it incurred \$15 billion in debt from CNPC, some of which was acquired in connection with CNPC's Sudan operations.
- CNPC is the privileged recipient of PetroChina earnings distributions; PetroChina's dividend distribution policy obligates it to share half of all earnings with CNPC.
- CNPC's pledge to isolate PetroChina from any Sudan-related operations - its so-called "Chinese Wall" - has clearly fallen apart; a cursory look at CNPC and PetroChina's relationship since the 2000 IPO demonstrates continuous and frequent transfers of assets between parent and subsidiary (and vice versa). In November 2005, PetroChina's chief financial officer went so far as to declare that PetroChina has a pre-emptive right to acquire Sudan assets currently held by CNPC.

Artificial Distinctions Between PetroChina and CNPC

At the highest levels, CNPC's and PetroChina's management significantly overlap, creating a parent-subsidary relationship generally alien to Western investors. Below are a few of the most troubling examples of this management overlap:

- In late 2006, Jiang Jiemin became the president of CNPC while retaining his position as president of PetroChina. He replaced the previous president of CNPC, who simultaneously served as PetroChina's legal counsel.
- PetroChina's directors also serve as CNPC's vice presidents.
- Only three of PetroChina's thirteen board members are non-executive and independent.

In its commentary, Berkshire compares the relationship between PetroChina and CNPC to the relationship between the US government and Fannie Mae/Freddie Mac. For the comparison to hold, the executive management of the US government and Fannie Mae/Freddie Mac would have to significantly overlap, which they do not. In fact, only 5 of the 18 board members of Freddie Mac are appointed by the President and shares in the company are not closely held by the US government (in contrast to CNPC, which holds well over 80% of PetroChina's shares). Furthermore, the types of fluid asset transfers that are so characteristic of the PetroChina-CNPC relationship do not exist in Freddie Mac/Fannie Mae's relationship with the US government.

Likely Outcomes if Shareholder Pressure on PetroChina/CNPC Intensifies

"The only feasible divestment plan for CNPC would be to sell its 40% interest in the venture, almost certainly at a bargain price and almost certainly to the Sudanese government."

--Berkshire Hathaway; Commentary on PetroChina holdings; February 21, 2007

Sudan does not presently have the capital or the expertise to buy and manage CNPC's 40% stake in Sudan's oil consortiums, even at bargain prices; the country's national debt well exceeds its GDP. Supposing Sudan could scrape together the capital to purchase CNPC's assets, its present revenue sharing relationship with CNPC would generate more income for the government than if Sudan's inefficient and resource-poor national oil company managed the assets on its own. The purchase of CNPC's assets would be bad business for Sudan. Since Sudan would be unlikely to purchase CNPC's stake, Berkshire's question "And then what [would happen if CNPC is forced to leave Sudan on account of external pressure]?" remains relevant. The most likely buyers of CNPC's assets would be the other two major oil players in Sudan, Malaysia and India's state-owned oil firms (Petronas and Oil & Natural Gas Company, respectively). While Sudan has benefited from the significant diplomatic cover China has afforded it as a permanent member of the UN Security Council (including China's active efforts to block deployment of a robust peacekeeping force to Darfur or sanction Khartoum), the governments of Malaysia and India simply cannot provide Sudan comparable political protection. *The sale of CNPC's Sudan assets would remove China's economic incentive to enable Sudan's ongoing genocide. Even short of forcing divestiture of its Sudan assets, pressure on CNPC is likely to change China's approach towards Sudan diplomacy, especially given how highly China prizes its Sudan's oil assets.*

The Sudan Divestment Task Force's Specific Request of Berkshire Hathaway

"We do not believe that Berkshire should automatically divest shares of an investee because it disagrees with a specific activity of that investee."

--Berkshire Hathaway; Commentary on PetroChina holdings; February 21, 2007

The Sudan Divestment Task Force agrees that *immediate* divestment is *not* Berkshire's most effective course of action in response to the Darfur genocide. Instead, the Task Force requests that Berkshire use its power and exercise its responsibility as PetroChina's largest US shareholder to rigorously engage the company in a sustained manner, seeking a firm commitment from PetroChina to work with its parent company, CNPC, to identify concerning operations in Sudan and implement safeguards to prevent PetroChina/CNPC actions from directly or indirectly contributing to the Darfur genocide. The Sudan Divestment Task Force has developed numerous specific suggestions for appropriate "asks" of PetroChina/CNPC, including:

- A halt to future expansion of operations in Sudan, including its exploration operations currently underway directly in South Darfur, until Khartoum fully complies with international obligations to protect its own citizens.
- Building a coalition with Sudan's other major oil-players (Petronas and Oil & Natural Gas Company) that collectively requests Khartoum allow a robust international peacekeeping force into Darfur.
- Meeting with Government of South Sudan officials and implementing their suggestions for sustainable operations. To date, CNPC/PetroChina has largely ignored the Government of South Sudan, even though much of its operations are on South Sudanese lands. This is in contrast to Western oil firms operating in Sudan which have, at minimum, considered the requests of both Khartoum and South Sudan in implementing operations plans.
- An immediate halt to unsustainable practices in the country, including published policies on handling graft in a country rife with corruption, prohibiting military vehicles from using company grounds for any operations, ending the forced displacement of local populations off of oil blocks, and condemning abusive actions taken by Khartoum to protect PetroChina/CNPC assets.

Because of the close interrelationship of PetroChina, CNPC, and the Chinese government (well-detailed in this document), the Sudan Divestment Task Force's request is clearly feasible and realistic. If PetroChina refuses to engage Berkshire in sustained and meaningful dialogue about its intimate affiliation with CNPC and CNPC/PetroChina's involvement in Sudan, Berkshire should then consider further action, including the possibility of divestment.