
Citigroup: a report on CSR policy and practices

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With a case study on Indonesia



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Introduction of the research

SOMO (the Centre for Research on Multinational Corporations) is a Dutch Non-Governmental Organisation which carries out different kinds of research for civil society use. Our company research in particular focuses on Corporate Social Responsibility (CSR) policies, and how these are applied in practice by the firm under investigation. In the period 2003-2004, SOMO has turned its attention to the financial sector, and has conducted research on two financial firms, the U.S. company Citigroup and the Dutch company ING Group. In the case of Citigroup, SOMO thought it was interesting to focus our research on the Asia Pacific region, and we selected researchers in Indonesia to conduct local investigations.

The research was carried out as part of our 4-year program 'Sector Research and Corporate Social Responsibility', and has been cofinanced by the Dutch Ministry of Foreign Affairs. The other financier of the research was Novib (Oxfam Netherlands).

The distinguishing factor of SOMO's research is that we often include case studies on the practice of CSR in our reports. For these case studies, SOMO has an extensive network of researchers in countries of the global South. SOMO also strives to maintain direct contact with those Headquarter employees which are responsible for CSR policies and practices in countries of the South during all company research.

Citigroup seems to have a comprehensive policy to incorporate CSR principles into its corporate culture and its daily operations. This SOMO report aims at identifying Citigroup's CSR policy and to assess how this policy is put into practice worldwide, and especially in Indonesia.

In Part 2 of this research paper, Citigroup's involvement in Indonesia is studied in depth. This case study is conducted by Business Watch Indonesia (BWI). BWI is an Indonesian NGO that was set up in 2002 to promote democratic economic governance. The research on Citigroup in Indonesia was conducted by BWI's own personnel, with the help of experienced Indonesian journalists. The report is based on desk research and on various telephone, e-mail and face-to-face interviews with Indonesian business analysts, social analysts, LonSum management and Citibank management and employees, which were conducted in the fall of 2003.

Glossary

Throughout this report, some words are underlined when they are used for the first time. These are the words that are explained in this glossary¹.

- Bonds: A debt instrument issued for a period of more than one year with the purpose of raising capital by borrowing. The investor loans money to an entity (company or government) that borrows the funds for a defined period of time at a specified interest rate.
- Broker: An individual or firm that charges a fee or commission for executing buy and sell orders submitted by an investor.
- Debt swap / debt to equity swap: A transaction in which a corporation exchanges newly issued stock for existing bonds. The debt holder gets an equity position in exchange for cancellation of the debt.
- Haircut: The difference between prices at which a market maker can buy and sell a security.
- Investment bank: financial institution that is in the business of raising capital for corporations and municipalities.
- IPO: The first sale of stock by a private company to the public. IPOs are often done by smaller, younger companies seeking capital to expand their business.
- Laddering: The promotion of inflated pre-IPO prices for the sake of obtaining a greater allotment of the offering.
- Mutual fund: A security that gives small investors access to a well diversified portfolio of equities, bonds, and other securities. Each shareholder participates in the gain or loss of the fund.
- Predatory lending: Any of a number of fraudulent, deceptive, discriminatory, or unfavorable lending practices. Many of these practices are illegal, while others are legal but not in the best interest of the borrowers.
- Security: An instrument representing ownership (stocks), a debt agreement (bonds), or the rights to ownership (derivatives).
- SEC (Securities and exchange commission): A government commission created by Congress to regulate the securities markets and protect investors.
- Shares (also called stock or equity): Certificates representing ownership in a corporation.
- Shareholder: Any person, company, or other institution that owns at least 1 share in a company.
- Spinning: The practice of brokerage houses exchanging IPO shares with top executives for reciprocating business from their companies.
- Subprime loan: A loan that is offered at a rate above prime to individuals who do not qualify for prime rate loans.

¹ Sources: www.investorwords.com, <http://economics.about.com/od/economicsglossary/index.htm>, www.investordictionary.com, www.investopedia.com, www.thefreedictionary.com, 23 June 2004

- Syndicate: A group of bankers, insurers, etcetera, who work together on a large project.
- Underwriting: The process by which investment bankers raise investment capital from investors on behalf of corporations and governments that are issuing securities (both equity and debt).

Bankruptcy: The legal process in which a person or firm declares inability to pay debts.

Brokerage firms: Financial services firms involved in the securities markets. They act as brokers, dealers, and investment bankers.

Financing: New funds provided to a business, by either loans or purchase of debt securities or capital stock.

Hedge fund: A private investment fund or pool that trades and invests in various assets such as securities, commodities, currency, and derivatives on behalf of its clients, typically wealthy individuals

Holding company: A corporation or other entity that owns a majority of stock or securities of one or more other corporations, thus obtaining control of the other corporations.

Balloon payment: A final loan payment that is considerably higher than prior payments.

Structured finance: A service offered by many large financial institutions for companies with very unique financing needs. These financing needs usually don't match conventional financial products such as a loan. Structured finance generally involves highly complex financial transactions.

Chinese Wall: A slang term for the barrier within a brokerage firm that prevents insider information from being handed out by corporate advisers to investment traders.

Fiduciary duty: the legal duty of a fiduciary to act in the best interests of the beneficiary

Brownfield sites (as opposed to greenfield sites): pieces of land that have once been developed, but that are now abandoned, like old industrial sites. Brownfield sites are often risky to redevelop, because of the possibility of soil contamination.

Letter of credit: A letter from a bank guaranteeing that a buyer's payment to a seller will be received on time and for the correct amount.

Market capitalisation: The total dollar value of all outstanding shares. It's calculated by multiplying the number of shares times the current market price. This term is often referred to as market cap.

PART 1: Citigroup and Corporate Social Responsibility (CSR)

1.1: Citigroup: an introduction

In brief

Citigroup Inc. is a United States based financial services company that combines banking, investment and insurance activities. It is the largest financial firm, and the fifth largest company in the world, if ranked by market capitalisation. At the end of 2003, its market value was \$259,190.8 million (or about \$259 billion U.S. dollars)². The company holds 200 million customer accounts in over 100 countries covering six continents, and employs around 275,000 people worldwide. Besides individuals, Citigroup provides financial services to corporations, governments and institutions. Citigroup's presence is strongest in the United States, Mexico and Japan. The company's headquarters are in New York City, and its logo is characterised by a red umbrella. Citigroup Inc. is listed on the New York Stock Exchange under the acronym 'C'.

Performance

Citigroup is doing well recently, despite the global economic downturn. Both its assets and its net income rose last year; assets went up from \$1.1 trillion in 2002 to \$1.3 trillion in 2003, and net income increased from \$15.3 billion in 2002 to \$17.9 billion in 2003³. For the period of 1999 until 2002, numbers were as follows⁴:

	2003	2002	2001	2000	1999
Total Assets (billions of U.S. \$)	\$ 1,246	\$ 1,097	\$ 1,051	\$ 902	\$ 796
Total Net Revenue (billions of U.S. \$)	\$ 77.4	\$ 71.3	\$ 67.4	\$ 63.6	\$ 54.8
Net Income (millions of U.S. dollars)	\$ 17,853	\$ 15,276	\$ 14,126	\$ 13,519	\$ 11,243
Return on Average Common Equity	19.8 %	18.6%	19.7%	22.4%	21.5%
Book Value per Share (U.S. \$)	18.79	\$ 16.60	\$ 15.48	\$ 12.84	\$ 11.23
Employees (full number)	253,000	250,000	268,000	233,000	212,500

Brand names

Among the most famous brand names under Citigroup's umbrella are Citibank, Travelers Life & Annuity, Smith Barney, Salomon Brothers, and Primerica. Other major brand names include Citi Cards, CitiFinancial, CitiMortgage, CitiInsurance, Citigroup Asset Management, the Citigroup Private Bank, Citigroup Alternative Investments, CitiCapital and Diners Club.

² Source: Financial Times Global 500, May 27, 2004

³ Source: Citigroup website, 'Corporate Governance', Annual Report 2003, www.citigroup.com

⁴ Source: Citigroup website, 'Investor Relations', financial snapshot, www.citigroup.com, 2 June 2004

Finally, the following well-known financial firms have been integrated into Citigroup: ‘The Associates’, or Associates First Capital Corporation; Bank Handlowy, a Polish bank; EAB, or the European American Bank; Golden State Bancorp, originally from California; Schroder from the United Kingdom and Banamex from Mexico.

People

The most important people within Citigroup are Sanford (Sandy) Weill, former CEO and currently Chairman of Citigroup; Charles (Chuck) Prince, the new Chief Executive Officer; Robert (Bob) Willemstad, President and Chief Operating Officer; Todd Thompson, the Group’s Chief Financial Officer; and Robert Rubin, Director and Chairman of the Executive Committee⁵.

Ownership

Besides its many fully owned subsidiaries, Citigroup, through its investment activities, has shares in dozens of U.S. and foreign companies, where its ownership typically ranges from 0.7% to 3.5% of all shares. Some examples within the U.S. are ALCOA (Aluminium Company of America, 2.8%), Amazon.com (1.8%), American Express (2.6%), AOL Time Warner (1.6%), Apple (1%), Walt Disney (1.8%), Enron (2%), Gillette 3.2%), IBM (1 %), Intel (1.5%), J.P. Morgan Chase (2%), Kimberly-Clark (2.8%), Mattel (2.7%), McDonalds (2.17%), Merrill Lynch (2.6%), Microsoft (0.98%), Motorola (1.6%), PepsiCo (1.33%), Safeway (2.1%), Texas Instruments (3.4%), and The Gap (1.7%).

Outside the U.S., Citigroup owns shares in Cadbury Schweppes (0.7%), CANTV (CA Nacional Telefonos de Venezuela, 1.6%), China Southern Airlines (0.8%), Electrolux (0.7%), Indosat (Indonesian Satellite Corporation, 0.7%), and Telecom Argentina STET (1.5%), amongst others⁶.

1.1.1: History

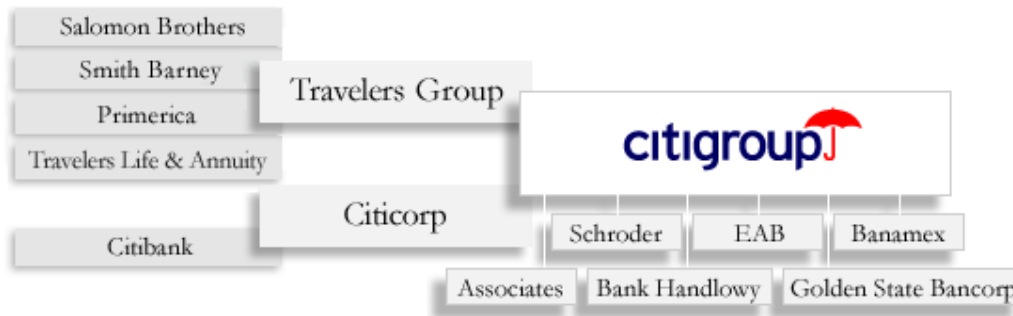
Citigroup came into existence in 1998 through a merger between the American banking and insurance giants Citicorp, the holding company of Citibank, and the Travelers Group. With the merger, Citigroup became the first financial services firm in the United States that combined banking, insurance and investment activities. This type of companies that cover the entire financial services spectrum is now often referred to as the ‘allfinanz’ business. The history of Citigroup is rather complicated because of the many mergers and acquisitions that took place, but understanding the historic antecedents of Citigroup does provide more insight in how the group operates today. The current Citigroup family tree

⁵ The following abbreviations will be used throughout this report: Chief Executive Officer = CEO, Chief Operating Officer = COO, Chief Financial Officer = CFO.

⁶ Source: Transnationale website, www.transnationale.org, 4 July 2003

largely reflects the history of Citicorp and Travelers Group before the merger, and of Citigroup after the merger:

Citigroup Family Tree⁷:



The left hand side of this diagram summarises the history of Citigroup before its own existence, and the right hand side gives an impression of developments since 1998. Apparently, the group’s history still has a large effect on its corporate structure.

Before the merger

Before the merger in 1998, both Citicorp and the Travelers Group had already come a long way in the financial industry. To get a good idea of the history of Citigroup, it is therefore helpful to look at the history of Citicorp’s and Travelers Group’s components, beginning with Citibank, the oldest of all Citigroup divisions⁸.

Citibank

Citibank was founded almost two centuries ago, on June 16, 1812 under the name ‘City Bank of New York’. Through a series of mergers, acquisitions and restructurings, the bank’s name changed to National City Bank, to First National City Bank of New York, to First National City Bank, and finally to Citibank in 1976. A few years earlier, in 1968, First National City Corporation, a bank holding company, had become the parent of First National City Bank. In 1974, First National City Corporation changed its name into Citicorp.

When mother company Citicorp merged with Travelers Group in 1998, Citibank continued to operate under its old name and became an important Citigroup brand. Citibank has been, and still is, an industry leader in various aspects. For instance, it was the first major bank to establish a foreign department in 1897, it had the first foreign branch of any U.S. national bank (in Buenos Aires, in 1914), and it was the first U.S. bank with \$1 billion in assets in 1919. More recently, Citibank’s financial leadership was affirmed when it became

⁷ Source: Citigroup website, ‘Corporate History’, www.citigroup.com, 2 June 2004

⁸ Source: Citigroup website, ‘Corporate History’, www.citigroup.com, 2 June 2004

the world's leading foreign exchange dealer (1979), the largest U.S. Bank (1992) and the largest credit card issuer in the world (1993).

Where Citicorp brought in Citibank, the Travelers Group added the following companies to the newly formed Citigroup in 1998: Primerica, Travelers Life and Annuity, Salomon Brothers and Smith Barney.

Primerica

Primerica's history can be traced back to the founding of the American Can Company in 1901 and the Commercial Credit Corporation in 1912. In 1987, the American Can Company changed its name into Primerica, and acquired investment broker Smith Barney. The following year, Primerica itself was acquired by Commercial Credit (where Sanford Weill was Chairman and CEO), and their parent company adopted the name Primerica Corporation. In 1993, Primerica acquired the Travelers Corporation and changed its own name into Travelers Inc. or Travelers Group, which became the new parent company. In 1997, Travelers bought Salomon Inc, and merged it with Smith Barney to form Salomon Smith Barney. In short, this is how the Travelers Group brought in Primerica, Travelers Life and Annuity, Salomon Brothers and Smith Barney.

Travelers Life and Annuity

Travelers Life and Annuity itself was born as 'The Travelers' in 1864 and started as a life insurance company. In 1899 it diversified into health insurance, and in 1967 the company entered the mutual fund business. In 1960 The Travelers adopted the red umbrella as its logo, which is still used today by Citigroup. Five years later, the insurance firm changed into The Travelers Corporation, a holding company of various subsidiaries, which was acquired by Primerica Corporation in 1993. Travelers had become a big name in the insurance business over the years. It was the first company to offer car insurance (1897), the first to offer life insurance to 'substandard' applicants (1906), and the first to have an Insurance Office of Consumer Information (1971). As said, with the acquisition in 1993, Primerica Corporation changed its name into Travelers Inc.. Primerica and Travelers Life and Annuity continued to operate as brand names of the newly formed Travelers Group.

Salomon Brothers

Salomon Brothers was founded in 1910 and experienced periods of growth both during the depression of the 1930s and during World War II, when it issued government bonds meant to raise money for financing the war. From the 1950's onwards it has been an innovator in the financial industry, using new technologies to expand its business. As mentioned, in 1997 Salomon Inc. was merged with Smith Barney and became a subsidiary of the Travelers Group.

Smith Barney

Smith Barney has its roots in Charles D. Barney & Co, founded in 1873, and Edward B. Smith & Co., founded in 1892. The two companies merged in 1938 and Smith Barney has provided brokering and investment banking services since. Smith Barney has retained its original name even when it became part of Citigroup in 1998, although over the years the names of Smith and Barney have been complemented on various occasions with the names of merged companies like Harris, Upman and Salomon. In 2003 Smith Barney employed about 12,400 financial consultants, managing almost \$900 billion in client assets.

The stories of these companies constitute the history of Citigroup until the merger of 1998. After the merger, some other companies joined the group through mergers and acquisitions. The most important acquisitions have been those of Associates First Capital Corporation ('The Associates') and Banamex.

After the merger

Associates First Capital Corporation

The Associates, an investment and insurance company, was founded in 1918. The company steadily grew and became an important provider of consumer credit in the United States. In the 1990s the company made dozens of acquisitions and became a financial industry giant with \$1.49 billion in net income: as a proof of their success, in 1999 The Associates recorded its 25th consecutive year of increased earning. On November 30, 2000 The Associates was bought by Citigroup.

Banamex

Banamex, or Banco Nacional de Mexico, was created in 1884 through a merger of Banco Nacional Mexicano and Banco Mercantil Mexicano. Throughout its history, the company has served as a commercial bank, but also as a commercial bank and a national bank in one, like during the first thirty years of its existence, from 1884 until 1926. It was privatised a second time in 1991, after it had served as a national credit association for almost ten years. During the events of 1991, Banamex merged with another bank and continued as Grupo Financiero Banamex-Accival, which was acquired by Citigroup in 2001. The transaction is the largest foreign acquisition in Mexico and the largest financial sector deal ever in Latin America. The following year, Citibank Mexico and Banamex were integrated and started operating under the Banamex brand name.

Other acquisitions

Other acquisitions of Citigroup have been Bank Handlowy w Warszawie (merged with Citibank Poland in 2001), the European American Bank (acquired from ABN Amro in 2001), Golden State Bancorp Inc. & California Federal Bank (acquired in 2002), and Schroder &

Co. (which was acquired in 2000, and merged with Salomon Smith Barney to form Schroder Salomon Smith Barney in Europe).

Recent history

Some important happenings in Citigroup's recent history have been:

- October 1999: former U.S. Treasury Secretary Robert Rubin joins Citigroup.
- November 1999: President Clinton signs the Financial Services Modernization Act, which leads to the recognition, in March 2000, of Citigroup as a financial holding company. This is important for Citigroup, because it makes it legal for the firm to operate as an allfinanz company, providing banking, investment and insurance services.
- Over the year 2000, Citigroup earns \$13 billion and becomes one of the most profitable companies in the world.
- On April 7, 2003 Citigroup renamed Salomon Smith Barney, and by extension Schroder Salomon Smith Barney in Europe: from that date onwards, all of its corporate and investment banking businesses operate under the name Citigroup Global Markets.
- October 2003: Charles O. Prince takes over from Sanford I. Weill as Citigroup's CEO. Sandy Weill will remain Chairman of the Board until the annual shareholder meeting in 2006.
- October 2003: Citigroup becomes the first bank that is allowed to trade commodities. This way, Citigroup can retain control over Phibro Inc., which it acquired in 1998 through the merger with the Travelers Group. Commodities traded by Phibro include "crude oil, refined oil products, natural gas, metals and various soft commodities"⁹.

1.1.2: Corporate structure and activities

Citigroup's many activities and branches are largely organised into five business groups:

- Citigroup Global Consumer Group;
- The Global Corporate and Investment Banking Group;
- Citigroup Global Investment Management;
- Smith Barney;
- Citigroup International¹⁰.

1: The Citigroup Global Consumer Group includes all Citigroup's consumer products, like banking activities, credit cards, personal loans and insurance:

⁹ Source: Phibro website, www.phibro.com, 9 July 2004

¹⁰ Source: Citigroup website, 'How Citigroup is Organized', www.citigroup.com, 2 June 2004

Citigroup Global Consumer Group:
<ul style="list-style-type: none"> • Citi Banking • Citi Cards • Citi Capital • Citi Financial • Primerica Financial Services

Besides banking, lending, investment and credit card services, through Citi Capital the Global Consumer Group provides truck, construction, material handling, healthcare, office equipment, franchise and municipal finance. The Consumer Group targets individual consumers and small businesses (up to \$10 million in annual sales)

2: The Global Corporate and Investment Banking Group provides financial services to corporations, governments, institutional and wealthy individual investors.

Global Corporate and Investment Banking Group:
<ul style="list-style-type: none"> • Global Equities • Global Fixed Income • Global Investment Banking and Global Relationship Banking • Global Transaction Services

Activities in this group include equity sales and trading, equity research, and retail brokerage; Fixed Income underwriting, structuring, sales and trading (including corporate, government and agency bonds and syndicated loans); foreign exchange and futures; advisory services regarding mergers, acquisitions, financial restructurings and all types of financial transactions; and specialised financial services to governments, institutions and corporations that operate on an international scale.

3. Citigroup Global Investment Management manages all types of investment, from public to private, and from small individual investors to large institutions.

Citigroup Global Investment Management:
<ul style="list-style-type: none"> • Citigroup Private Bank • Citigroup Asset Management • Global Retirement Services • Travelers Life and Annuity • Citigroup Alternative Investments

Some of the activities in this group are: personalised wealth management; mutual fund, private and institutional portfolio management; health and welfare services to corporations and organisations; life insurance and annuity products (e.g. asset protection, retirement planning); alternative investment services such as hedge funds, private equity and other special investment opportunities.

4. Smith Barney is Citigroup’s private wealth management and equity research unit. The company provides financial consultancy services to wealthy private investors, institutions, corporations, governments and organisations. Wealth management can take the form of asset allocation, investment and lending services, hedge funds, cash and portfolio management and other financial services. Smith Barney is a division of Citigroup Global Markets.

5. Citigroup International refers to the international operations of Citigroup. Outside the U.S., the Group concentrates mainly on banking, lending, investment and insurance activities aimed at individual consumers. But Citigroup also provides treasury, foreign exchange and financial advisory services to individuals, businesses, governments and institutions worldwide.

Besides this division in five groups, which does not seem to be based on any specific criteria, Citigroup has also organised itself along nine product lines¹¹:

Product line	Business Group
<ul style="list-style-type: none"> • Cards • Consumer Finance • Retail Banking 	Citigroup Global Consumer Group
<ul style="list-style-type: none"> • Capital Markets & Banking • Global Transactions Services 	Global Corporate and Investment Banking Group
<ul style="list-style-type: none"> • Life Insurance and Annuities • Private Banking • Asset Management 	Citigroup Global Investment Management
<ul style="list-style-type: none"> • Private Client Services 	Smith Barney
<ul style="list-style-type: none"> • All product lines 	Citigroup International

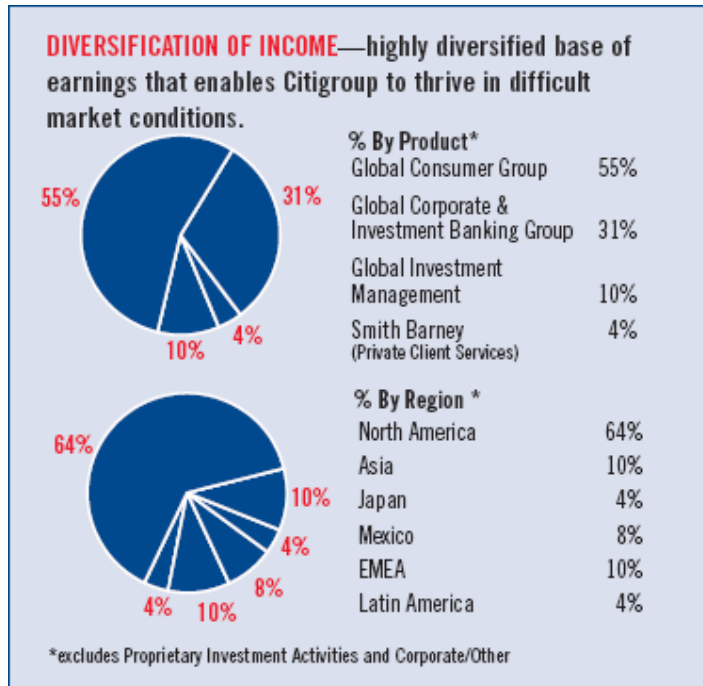
As the table shows, each business group offers one or more of these product lines. Only Citigroup International manages all of these product lines, because it carries responsibility for all of Citigroup’s activities outside North America.

The categorisation of activities along product lines is important because it reflects the company’s reporting lines. However, besides reporting by product line, Citigroup also reports by geography, differentiating between six, rather artificial, regions:

- North America
- Mexico
- Europe, Middle East and Africa (EMEA)
- Japan

¹¹ Source: Citigroup website, ‘Citigroup’s Nine Product Lines’, www.citigroup.com, 2 June 2004

- Asia
- Latin America



This table from the Annual Report 2003 gives some insight into the relative size of the company's activities and regions¹².

All in all, it can be said that it is very difficult for outsiders to get a clear idea of how the financial giant is organised, and who is responsible for what within the company. As said, reporting lines run along product lines and geographical regions, but it does not become very clear from Citigroup's public information channels (website, annual report, various corporate governance and Corporate Social Responsibility reports) who carries specific responsibility at the various management levels of the organisational groups, product lines and regions. The whole corporate structure seems a little chaotic.

1.1.3: Rankings

According to the Financial Times, Citigroup is the largest bank in the world¹³, and the fifth largest company worldwide¹⁴, if ranked by market capitalisation only. Currently, in 2004, Citigroup is far ahead of the second largest bank in the world, the British HSBC bank, who's market value stands at \$ 163,573.8 million, compared to Citigroup's market value of \$ 259,190.8. But because of the many mergers and acquisitions that still take place within

¹² Source: Citigroup website, Annual Report 2003, p. 3, 2 June 2004

¹³ The newspaper makes a bit of an awkward distinction between banking and insurance firms, which creates a problem with the ranking of allfinanz firms like Citigroup and for instance the Dutch ING Group. Both are allfinanz companies, but Citigroup is ranked in the banking sector and ING in the insurance sector

¹⁴ Source: Financial Times Global 500, May 27, 2004

the industry, the number 1 position might be less firmly established than one would suspect from the current status quo.

Also in 2004, Citigroup ranks #1 on the new Forbes 2000 list of the world's biggest companies, measured by a composite of sales, profits, assets and market value. It also held this position in 2003 and in 2002, when the list was called Forbes 500. On Forbes' list of the richest people in the world, Sanford Weill, Citigroup's former CEO, ranks #377 in 2004, personally being worth about 1.5 billion dollars¹⁵.

In Citigroup's own Annual Report, a whole list is given of the Group's number 1 rankings in 2003. Some examples are: Best Cash management Bank in Asia (Asiamoney), Best Bank/Commercial Bank/Investment Bank/Foreign Exchange Bank in Asia (The Asset), Best Overall Service in Latin America, North America (The Banker), World's Best Bank for Cash Management & Payments (Euromoney), and a whole list of Best Bank and Best Loan House awards from the Global Finance, Treasury Management International and International Financing Review magazines. According to the company's own CEO and COO, Citigroup is "the largest and most profitable bank in the world"¹⁶.

Citigroup is the world's largest provider of credit cards and the number one underwriter of Combined Debt and Equity related transactions¹⁷.

1.1.4: CSR ratings

Negative ratings

Unfortunately for Citigroup, the company did not only get positive rankings. In 2000, the World's Most Destructive Bank Award was invented by a number of NGO's as part of their campaign against Citigroup, which obtained this award, amongst other reasons, because that year the company was the world's largest financier of oil pipelines and the coal industry, and the world's second largest funder of mining, forest and paper products, according to Bloomberg research¹⁸. (Bloomberg is an important source of information on global capital markets; it provides news and analysis on TV, radio, internet, magazines and through the press).

The next year, in 2001, Bloomberg found that Citigroup was the largest financier of the coal industry and the fossil fuel industry, both of which are notorious for their contribution to the increase in the world's greenhouse gasses which ultimately leads to global warming.

¹⁵ Source: Forbes website, www.forbes.com, 7 June 2004

¹⁶ Source: Citigroup website, 'Corporate Governance', Annual Report 2003, www.citigroup.com, 2 June 2004

¹⁷ Source: Citigroup website, 'How Citigroup is Organized', www.citigroup.com, 2 June 2004

¹⁸ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

In 2002, the *Multinational Monitor*, a monthly magazine on corporate behaviour, put Citigroup in its annual top ten list of the world's Worst Corporations, because of the many scandals Citigroup was involved in that year, including misleading Wall Street research, predatory lending practices and the financing of environmentally destructive projects around the world.

Positive ratings

But strangely enough, almost simultaneously, Citigroup also was included in some important positive CSR rankings. It was included in the Dow Jones Sustainability World Index both in 2003 and in 2004. The DJSI is a list of about 300 companies worldwide that represent the top 10% of the biggest 2500 companies from the Dow Jones Global Indexes when it comes to corporate sustainability¹⁹. Another sustainability index, the FTSE 4 Good Index, which is put together by the Financial Times and the London Stock Exchange, also included Citigroup in 2003 and in 2004. The index only includes companies that meet specific environmental, social and financial criteria²⁰.

Even more surprising, in June 2003, Citigroup made its entrance in the top 20 ranking of the most frequent stocks in European green, social and ethical funds portfolios, where it came in at number 4, only after Vodafone, Pfizer, and Johnson & Johnson. The ranking of most frequent stocks in European Socially Responsible Investment (SRI) funds portfolios was put together by Avanzi SRI Research and the SiRi Group, two research organisations that jointly publish a "Green, Social and Ethical Funds in Europe" survey each year. Companies only qualify for SRI funds if they pass a number of ethical, social and environmental requirements.

The sudden entry of Citigroup in the top 20 of European SRI portfolios and its inclusion in two important sustainability indexes raises the question how a company, which has been condemned in the recent past by various organisations for its lack of corporate, social and environmental responsibility, can occupy such a high place in positive CSR rankings. It suggests that either the rankings do not adequately reflect the company's CSR record, or that Citigroup has suddenly made a major turn-around when it comes to its CSR policy. Which of these possibilities is true, is a question that is addressed in the following section.

1.2: Citigroup and CSR: policy, implementation and commitments

Since the late 90s, financial services companies, which had typically stayed outside the realm of much of the public debate on Corporate Social Responsibility, have increasingly become the target of public campaigns that point attention to their social responsibilities as important economic actors. Worldwide, Non-Governmental Organisations, and many

¹⁹ Source: <http://www.sustainability-indexes.com/>, 10 June 2004

²⁰ Source: Citigroup website, 'Corporate Governance', Annual Report 2003, p. 26. www.citigroup.com, 2 June 2004

other interest groups, have come to realise that the financial sector is not only the single largest economic sector, but that it also carries the greatest responsibility for the allocation of financial resources, which are at the basis of all economic activity. Basically, financial sector actors decide which business operations get funded, and which don't. Therefore, if the world is to move any closer to sustainability, financial services firms will have to redefine their role in economic society.

Financial firms like Citigroup acknowledge their duties to the economy, the environment and society at large in their Corporate Social Responsibility policy. Some firms take on greater responsibilities than others. The following section describes where Citigroup stands on important CSR issues.

1.2.1: CSR Policy

Before NGO's and special interest groups came along to point out financial firms' social and environmental responsibilities, the area on which public debate and national and international regulation and legislation for the financial sector had traditionally focused was that of 'corporate governance'. Corporate governance is a term that basically refers to *the way* business is done, or to the *internal* responsibilities of a company. In a narrow sense, corporate governance addresses issues like corruption, fraud, bribery, conflicts of interest and violations of privacy. If a company adequately addresses these issues and conducts its core business according to the basic 'rules of the game' which are accepted within a society, this is considered good corporate governance.

More recently, the corporate governance debate has concentrated mainly on issues of *transparency* and *accountability*. Both terms have to do with the way a business relates itself to its *stakeholders*, or the people that take an interest in the way the company functions. Stakeholders are usually defined as all shareholders, clients, employees, public authorities and society at large. Some of the corporate governance issues stakeholders have raised over the last few years are the level of shareholder control over a company, executive compensation, and the proper disclosure of corporate information.

Besides corporate governance, companies are increasingly judged on their *corporate citizenship* performance. Corporate citizenship refers not so much to *how* business is done, but rather focuses on *the kind* of business that is done, that is, to the *external* responsibilities of a company. Is the company involved with the use of child labour, or with environmentally unsound business practices? Does the company pay attention to social equality issues, for instance by making sure that socially disadvantaged groups like the elderly, the handicapped and people of colour have equal access to the firm's services? Is the company actively promoting sustainability and social justice? In short, corporate citizenship refers to the way a company takes responsibility not only for its internal actions, but also for the external effects of its operations on society.

The distinction between corporate governance and corporate citizenship is not a commonly used one, and sometimes poses problems, because corporate governance and corporate citizenship issues may overlap.

In this SOMO financial sector report, both areas of corporate conduct are seen as part of Citigroup's Corporate Social Responsibility policy. Normally, however, the NGO community, including SOMO, do not regard all corporate governance initiatives treated here as part of CSR policy. The CSR debate has generally focused on corporate citizenship issues, and only recently has incorporated corporate governance issues. In the Netherlands, for instance, an NGO network working on CSR agreed to focus the CSR discussion on the following issue areas²¹:

1. human rights
2. labour
3. environment
4. consumer protection
5. health
6. corruption
7. other CSR aspects: competition, taxation, science and technology, respect for national sovereignty and communities.

In addition, the Dutch CSR Frame of Reference states the following operational aspects of CSR that should be included in companies' CSR policies:

1. supply chain responsibilities
2. stakeholder involvement
3. transparency and reporting
4. independent verification

This shows that the general discussion on CSR does make a distinction between an effect-based category of CSR issues (corporate citizenship) and operational aspects of CSR (corporate governance), but includes issues such as corruption, competition and taxation in the first category, whereas this report rather views these issues as corporate governance aspects.

The difference in interpretation is largely due to the specific character of the financial services sector. In this business area, corporate governance issues are a much more important part of corporate responsibility than in many other sectors. Especially issues like conflicts of interest and consumer privacy protection play a different, and much bigger role in the financial services sector than in most other productive sectors. Therefore, the distinction made in this report between corporate governance and corporate citizenship

²¹ Source: MVO Platform, CSR Frame of Reference, <http://www.mvo-platform.nl/mvotekst/CSR%20frame%20of%20reference.pdf>, 9 July 2003

seems to make sense from both a theoretical and a practical point of view. The two areas of Citigroup's Corporate Social Responsibility will be described briefly in the following sections.

1.2.1.1: Corporate Governance

Citigroup has published four important documents that reflect its corporate governance policy: the Code of Conduct, the Corporate Governance Guidelines, the Code of Ethics for Financial Professionals and the Citigroup Initiatives on Corporate Governance and Business Practices. The first two documents have been around for a while, but are still regularly updated to reflect new trends in corporate governance or to adapt to new legislation regarding corporate governance issues. The Code of Ethics is a new document that was released in 2003 in an effort to reaffirm and revitalize the company's Code of Conduct. The Citigroup Initiatives on Corporate Governance and Business Practices document was published in the spring of 2003 to provide a summary of the many changes Citigroup made to its corporate governance policy in 2002. This document will be discussed in section 1.2.3.

Besides these papers, important aspects of the Group's corporate governance policy and practice are usually mentioned in the Citigroup Annual Report, and policy changes are also summarised in the annual Corporate Citizenship Report. Finally, the Group's corporate governance policies are described on the company website.

The Code of Conduct

The Code of Conduct basically is a summary of all the principles, policies and laws that Citigroup's own employees must adhere to. It is a guide for behaviour for all employees of Citigroup, Citigroup subsidiaries and affiliates. The document is centred around six main points:

1. employees' responsibilities
2. workplace responsibilities
3. representation of Citigroup to the outside world
4. privacy and confidentiality
5. investments and outside activities
6. Other key legal and compliance rules and issues

The first point treats issues of accounting, compliance with laws and internal regulations, the use of Citigroup assets, and the contents of Citigroup records, including e-mail. Employees are made responsible for their own and each others' conduct, and are supposed to behave in an ethical manner during work time. If employees know of a (possible) breach of laws, regulations or internal policy within the company, they are expected to warn the person in charge with compliance, for instance through Citigroup's own Ethic Hotline, which is available 24/7, and treats calls anonymously.

Secondly, the Code of Conduct identifies Citigroup's policies regarding the workplace. According to this point, Citigroup is committed to having a diverse workforce, to fair employment practices, to the elimination of discrimination, harassment and intimidation at the workplace, to the safety of employees and to a drug free working environment.

As to the representation of Citigroup to customers and other external parties, the Code of Conduct states that all customers, suppliers and competitors will be treated fairly, and that all external communications must be approved internally prior to their release. Point three also treats the important issues of corruption, bribery and lobbying. Accepting and giving gifts is not permitted, unless it complies with strict internal regulations. Also, the Group supports the Foreign Corrupt Practices Act which prohibits donations to foreign government officials, and furthermore employees lobbying on a national level on behalf of the Group are expected to get prior consent from the Group. However, "most political activities must be undertaken as a private individual, not as a Citigroup employee"²².

The fourth point binds employees to protecting confidential information in accordance with the law and with Citigroup's own 'Privacy Promise for Consumers'. And, very importantly for an allfinanz business, the Group promises to respect information barriers between employees engaged in lending, investment banking and merchant banking activities and employees who trade in securities or engage in investment management, to avoid a conflict of interest between Citigroup's various divisions.

In the fifth point, reference is made to trading in Citigroup securities by employees, which is classified illegal if done on the basis of non-public information, and to additional insider trading restrictions for employees of certain Citigroup business units.

Finally, in a kind of 'miscellaneous' section, the Code of Conduct sums up a number of rules and regulations that employees have to abide to, ranging from anti-money laundering programs to anti-boycott laws. More specifically, the last point of the Code identifies 10 additional duties for employees, namely statements on the following subjects:

- Fair and free markets: employees may not manipulate the markets in which they operate;
- Tied business dealings: employees should be careful to make arrangements whereby one transaction is made a condition for another, because this can sometimes be illegal;
- Antitrust compliance: all applicable laws must be respected;
- Environment: employees should assess the environmental risk of their operations and implement Citigroup's environmental commitments;

²² Source: Citigroup website, 'Corporate Governance', Code of Conduct, p. 2. www.citigroup.com, 2 June 2004

- Anti-money laundering: employees must act in accordance with the Group’s Global Anti-Money Laundering Policy, and are expected to be aware of their customers’ reputation;
- Suspicious activity reporting: employees have to make sure suspicious or illegal activity is reported to government authorities;
- Financial holding company restrictions: before acquisitions, investments, divestitures, or the introduction of new products or services take place, employees must consult with their business unit’s internal counsel to make sure relevant banking laws are not violated;
- Anti-boycott laws: Citigroup employees may not support any boycott of a country that is considered friendly to the U.S.;
- U.S. embargoes and sanctions: the company complies with economic sanctions and embargoes that are aimed at terrorist activity and narco-trafficking.
- Structured finance: employees must comply with the Citigroup Structured Finance Policy, which promotes transparency on this kind of transactions.

All in all, the Code of Conduct should guarantee the personal and professional integrity of all Citigroup’s employees, independent contractors and consultants, all of whom are expected to read the Code and act in accordance with it. A critical note about the Code is, that the division between the six areas of conduct is not always a very clear one, and that some areas pile together seemingly unrelated issues. This leads to a situation where very important aspects of the Code do not get the attention they deserve. One recommendation could be to make separate categories for bribery, corruption and lobbying on the one hand, and for information barriers between business activities on the other. These issues could better be treated in their own right, instead of as ‘external representation’ and ‘privacy’ issues, respectively.

The corporate Code of Conduct reveals a bit more about the internal communication lines and lines of responsibility than do other public sources of information about the Group. From the text, it becomes clear that the following people are responsible for compliance with the Code: each business unit’s Internal Counsel, Compliance Department, Risk Department and Human Resources Representative; the Citigroup Global Compliance Office; the General Counsel; and the company’s Audit and Risk Review. Outside the U.S., Country Officers and Regional Public Affairs Officers also play a role in assuring compliance with internal and external rules and regulations.

Furthermore, in the U.S., there are various offices in place that are responsible for Citigroup’s policy on, and implementation of, specific CSR issues and regulations, including but not limited to corporate governance issues. These are: the office of Environmental Affairs, the office of Corporate Governance, the Corporate Public Affairs Office, the Government Affairs Office, the Corporate Security and Investigative Services, the Anti-Money Laundering Unit, and the office of Investor Relations.

Since 2003, at the corporate level and within each business unit, there is a separate ‘Business Practices committee’, which identifies potentially problematic business practices within its unit and reports on these to senior executives, who judge whether or not the CSR policies that are already in place are appropriate. Issues for the business practices committee report may be raised by all personnel.

Other interesting aspects of the Code of Conduct are:

- All employees are expected to cooperate fully with any internal or external investigation;
- Employees are prohibited from destroying any records that may be relevant to real or possible investigations;
- “No person may take unfair advantage of anyone through manipulation, concealment, abuse of confidential information, misrepresentation of material facts or unfair dealing practice”²³. One way to assure this is compliance with national and international fair lending standards and Citigroup’s own fair lending policy.
- Suppliers and service providers of Citigroup are expected to respect Citigroup policies and have to meet the company’s Approved Supplier Policy;
- Citigroup’s Political Action Committees (PACs) are funded by personal contributions by employees and are the “only permissible sources for funding U.S. political contributions on behalf of Citigroup”²⁴;
- Lobbying activities require prior consent of the Government Affairs Office, and outside the U.S. also of the Country Officer. Lobbying can take the form of an attempt to influence the outcome of legislation, or of influencing government financing decisions.

The Code of Conduct was revised in 2003 to incorporate a number of important changes that were made necessary after some financial scandals had rocked consumer and investor confidence in Citigroup in 2002. The new version was introduced to employees through an online training program called “Know the Code”, which was offered in 13 languages²⁵.

In conclusion, the present Code of Conduct is a good indication for employees how to behave during work time. Each point of the Code stresses that if any questions or doubts regarding professional conduct remain for personnel, they are required to discuss the matter with their supervisor or the person who is in charge of the issue before taking action. This provision makes sure that all areas of conduct are effectively covered by the

²³ Source: Citigroup website, ‘Corporate Governance’, Code of Conduct, p. 8. www.citigroup.com, 2 June 2004

²⁴ Source: Citigroup website, ‘Corporate Governance’, Code of Conduct, p. 10. www.citigroup.com, 2 June 2004

²⁵ Source: Citigroup website, ‘Corporate Governance’, Citizenship Report, www.citigroup.com, 2 June 2004

Code, leaving no excuse to employees who cross the borders of what is considered acceptable behaviour.

The Corporate Governance Guidelines

Within Citigroup, there is one group of employees which is not subjected to direct internal supervision by superiors with regard to ethical behaviour. This group has no superiors because it stands at the top of the company's hierarchy: it is the Board of Directors. For them, an additional document, called the Corporate Governance Guidelines, outlines the limits of what is considered acceptable. The guidelines treat issues such as the number and selection of Board Members; Director Independence; Director Compensation; the Chairman, CEO and COO performance review; and Insider Transactions. The Nomination and Governance Commission is mentioned as the main body that monitors the performance of the Board, The current Corporate Governance Guidelines have been effective as of March 2004²⁶.

Some specific rules the Corporate Governance Guidelines set out have just recently been established, like the "interlocking directorates" rule, which states that no internal Director of Citigroup may also serve as a director of another company where a Citigroup outside Director is an executive officer. Another new rule states that Director and their families may no longer receive Initial Public Offering (IPO) allocations, because this could be considered as favouring Directors over other investment clients. These corporate governance reforms were made after a lot of turmoil in the financial world in the early 2000's, when the integrity of banking and investment firms and their executives was called into question.

The Code of Ethics for Financial Professionals

The last corporate governance document to be treated here is Citigroup's two page Code of Ethics for Financial Professionals. It applies to "the principle executive officer of Citigroup and its reporting subsidiaries and all professionals worldwide serving in a finance, accounting, treasury, tax or investor relations role"²⁷. The Code of Ethics is a supplement to the Code of Conduct and must be signed by the financial services employee and handed in to his or her manager or human resources representative. It was adopted in January 2003, after a number of controversial accounting practices and financial fraud issues had severely damaged the reputation of Citigroup's financial professionals.

The Code consists of six points that the employee agrees to adhere to, namely that he/she will: engage in and promote ethical conduct; avoid conflicts of interest; treat information

²⁶ Source: Citigroup website, 'Corporate Governance', Corporate Governance Guidelines, www.citigroup.com, 2 June 2004

²⁷ Source: Citigroup website, 'Corporate Governance', Code of Ethics, p. 1. www.citigroup.com, 2 June 2004

in a confidential manner; “Produce full, fair, accurate, timely, and understandable disclosure in reports and documents [...]” which are filed with, or submitted to, “the Securities and Exchange Commission and other regulators and in other public communications [...]”²⁸; comply with all applicable laws, rules and regulations, whether internally or externally imposed; and report any possible violation of the Code of Ethics. Two final clauses explicitly state that employees are prohibited from misleading independent public auditors and that they can personally be held accountable for breaches of the Code. Basically, the Code of Ethics does not add anything new to the Code of Conduct, but it is more clear on the specific do’s and don’ts for financial services providers.

The Annual Report

In their opening letter of the Annual Report 2003, Citigroup’s CEO and COO, Chuck Prince and Bob Willumstad, emphasize three aspects of the company’s CSR policy: that the policy is intended to earn the trust of customers and the respect of regulators; that CSR should be embedded in corporate business and in corporate culture; and that Citigroup wants to be an industry leader when it comes to Corporate Social Responsibility. Prince and Willumstad state that “Because of our size and scope, because of the benefits of our position of business leadership, we are held to a higher standard. We accept this responsibility”²⁹. The overall goal of the company is to be “the most profitable, most respected financial services company in the world”. As for their employees, the heads of Citigroup “value a culture of accountability”³⁰.

In the Annual Report, each division of Citigroup provides a short description of its overall performance over the last year. In the 2003 report, only the Global Consumer Group, the Global Corporate & Investment Banking Group and Smith Barney make a specific reference to corporate governance policy. This reference is invariably very general and brief and only describes the most important policy changes that have been made over the past year, without much explanation why adjustments were made or how they will be implemented.

The Annual Report is therefore considered rather weak on corporate governance issues. It does not refer to any of the corporate governance problems that have plagued the company in 2002 and 2003, and it only lightly touches upon the remedial measures that have been taken to restore confidence in the company’s integrity. While the whole report emphasises that Citigroup wants to be an industry leader when it comes to ethical governance, it does not elaborate much upon the specific means to this end. No clear and inclusive list of problematic issues and accompanying policy measures is given. Considering that the report is meant to provide a summary of the Group’s performance to

²⁸ Source: Citigroup website, ‘Corporate Governance’, Code of Ethics, p. 1. www.citigroup.com, 2 June 2004

²⁹ Source: Citigroup website, Annual Report 2003, p. 6. www.citigroup.com, 2 June 2004

³⁰ Source: Citigroup website, Annual Report 2003, p. 7. www.citigroup.com, 2 June 2004

shareholders, this is rather disappointing. Surely, shareholders are not only reassured by strong financial performance, but also want to know more in detail about the continuing reputation risks Citigroup is facing, and the measures the Group is taking to regain its trustworthiness.

The Global Corporate Citizenship Report

The Citizenship Report 2003 devotes one page to corporate governance issues, and focuses mainly on the changes that have occurred in the last year. Apart from the changes that have already been mentioned, like the update of the Code of Conduct, for 2003 the report also notes that Citigroup began reporting its quarterly financial statements using only GAAP (Generally Accepted Accounting Practices) income measures. For the specific changes Citigroup made in its corporate governance policy regarding accountability and transparency, the Citizenship Report refers to the Citigroup Initiatives Corporate Governance Business Practices report, which will be treated in section 1.2.3.

The company website

Citigroup's website describes the company policy on the following corporate governance issues, which will be described below:

1. Consumer finance
2. Structured finance
3. Equity research
4. IPO allocations
5. Money laundering
6. Privacy

Consumer finance

The consumer finance section focuses on Citigroup's sub-prime lending services, which are provided by CitiFinancial. Sub-prime lending provides a source of credit for people who do not normally qualify for traditional bank loans, such as Citibank or CitiMortgage loans. These people constitute a higher risk to the lender and therefore, sub-prime loans are more expensive than regular loans. When such loans become really expensive, are sold in an unethical manner, and are likely to get consumers into financial trouble, this is called 'predatory lending'.

Since 2000, Citigroup senior staff and CitiFinancial staff have been working to improve the company's consumer finance policy. This was necessary because of a number of allegations against Citigroup, accusing the company of taking advantage of the economically weak sectors of society, like black communities and elderly people, since the Group's acquisition of Associates First Capital Corporation. The Associates was generally known for its bad track record on predatory lending. As part of the company's 'CitiFinancial Lending

Initiatives and Enhancements' program, the Group says it has now reduced the maximum points on real-estate loans from 5 to 3 (which means it has lowered the maximum lending fee), and that it has stopped selling a controversial insurance product, namely the personal property insurance³¹.

Besides this, Citigroup says it will make sure no clients will unnecessarily be stuck with expensive loans, because interest rates will automatically reduce for people who improve their credit. If clients meet prime credit criteria they will be referred to CitiBank and CitiMortgage where they can get a cheaper loan than from CitiFinancial. Also, the refinancing of debt will no longer be used to trick people into more expensive loans, but will have to provide a tangible benefit to the customer. Apart from these improvements, Citigroup promises to steer clear from controversial lending practices like 'balloon loans', and assures it will not engage in any form of discrimination of its clients.

These and other new standards will be monitored in various ways, for instance by a 'mystery shopper', who unexpectedly checks on insurance salesmen. A customer Hotline will be opened for complaints, and dispute settlement will take place through arbitration. CitiFinancial employees will receive training on fair lending, business ethics and insurance sales techniques. A compliance staff will regularly audit each branch office. All applicable laws, including the Truth in Lending Act, the Fair Housing Act, and the Patriot Act, will be respected.

It seems like Citigroup has really taken consumer complaints seriously and is working hard to end the trouble that The Associates have caused in the last few years. This aspect of their corporate governance policy can therefore be judged positively.

Structured finance

The structured finance section deals with specific accounting services Citigroup provides to its corporate clients. Citigroup has come into trouble in the past few years because it helped large companies like Enron and Dynegy to hide their debt, making shareholders and the public believe that the companies were doing well, while they really were on the verge of bankruptcy.

After investigations, Citigroup actually agreed to settle accusations and paid several fines for its involvement in structured finance work (see section 1.3.1.4). It has now reformed its policy to avoid similar accusations in the future. The emphasis of this reform is on transparency. Citigroup says that from now on, it will only work with companies that publicly disclose the net effect of structured finance in their financial statements³².

³¹ Source: Citigroup website, 'Corporate Citizenship', Consumer Finance, www.citigroup.com, 2 June 2004

³² Source: Citigroup website, 'Corporate Citizenship', Structured Finance, www.citigroup.com, 2 June 2004

With the ‘net effect’ rule, Citigroup is taking the lead within the financial industry, and prospects are good that the company will refrain from using similar doubtful accounting practices in the future. Since the recent structured finance scandals, the company is under constant public scrutiny. Citigroup knows by now that their client’s accounting malpractices have a direct effect on the Group’s reputation, and that no client is worth this risk.

Equity research

Since the merger of Citicorp and Travelers Group in 1998, Citigroup has been an allfinanz business combining banking, investment and insurance services. Investment banking and equity research have usually been separated by law because combining the two activities can lead to a conflict of interest. The problem is that companies listed on the stock exchange are judged by research analysts, and their judgement may influence the success of the company. Analysts therefore have to be independent and provide objective information on these companies’ merits. But in an allfinanz business, the same companies that are judged by analysts may also be clients of the financial firm’s corporate banking division. Positive ratings on companies may be beneficial to the bank. This is a serious conflict of interest that must be adequately addressed by each allfinanz business, and it rather surprising that there was so little control over this issue in the first years of Citigroup’s existence.

A number of scandals that were brought to a light in the past three, four years have drawn attention to the issue of independent equity research. Citigroup was sued, along with nine other financial firms, and had to pay the largest penalties of the ten firms, in 2003. In an effort to raise investor confidence, Citigroup has taken a host of measures last year to establish so-called “Chinese Walls” between its investment banking and research divisions.

According to the Citigroup website, there now a permanent prohibition to promise favourable research to companies in return for investment banking business. The equity research unit of Citigroup, Smith Barney, is not allowed to report to the investment banking division. The compensation for research analyst may only depend on the benefits the analysts have provided to investor clients, not on the successes they have brought the investment banking division³³. These and other rules regarding independent equity research are all so obvious that it seems unbelievable that Citigroup has not lived up to them before nation-wide scandals forced them to take analyst independence seriously. From now on, however, it can be expected that Citigroup will follow up on its promises and will not risk its reputation again this way.

IPO allocations

³³ Source: Citigroup website, ‘Corporate Citizenship’, Equity Research, www.citigroup.com, 2 June 2004

An Initial Public Offering is the first sale of equity by a company to shareholders. This happens when a previously private company is listed on the stock exchange, or 'goes public'. Until the late 90s, it was quite difficult for a company to be qualified for a listing on the stock exchange. But the internet hype of the late nineties lowered the standard for companies to go public. Small new companies tried to raise quick cash by doing an IPO. The cash raised from investors was meant for the expansion of the company, but often these new 'dotcom' companies did not manage to make a profit at all and went bankrupt, having made their founders and brokers rich in the meantime³⁴.

IPOs are done by investment banks, which take care of the formalities of a new listing and sell stock to the public, a process known as 'underwriting'. They get a fee from the company they work for, and the higher the price they get for IPO stocks, the more money they make. The brokers that work at investment banks are basically salespeople, trying to sell stock. Just before the IPO, brokers go on road shows to get large investors interested in the new stock. Roadshows are a marketing tool intended to create a hype around an IPO, in order to drive up the price of the stock.

The late 90s were a time of great economic optimism and consequently a real rush on IPOs, especially from dotcom companies. The hype lasted until March 2000; after that, the internet bubble burst, only few dotcom companies survived, and investors lost millions of dollars. It became clear that during the hype, many investment banks had engaged in activities which were not prohibited, but could definitely be considered unethical. Investment banks have a responsibility to protect their investors, but they had massively failed to live up to their fiduciary duty.

Citigroup, through its investment banking division, had been an active underwriter of IPOs during the internet hype. The specific ethical problems with IPO allocations will be discussed in section 1.3.1.2. Broadly, it can be said that 'hot' IPO stocks were preferably given to insiders and corporate business partners, who could make a lot of money selling these. Meanwhile, the conflict of interest between investment banking and equity research was also applicable to the allocation of IPO shares. Market analysts were fuelling the internet hype with their unjustifiably positive ratings for dotcom IPOs. Since 2002, some policy changes have been implemented to stop preferential IPO allocation and to separate research and investment banking activities.

Citigroup has promised that its research unit Smith Barney will no longer report to its Investment Banking Division. Market analysts and brokers may no longer promise favourable research or IPO allocations in return for investment banking business. Another important improvement is that Citigroup is working on an industry wide ban on the

³⁴ Source: online investment encyclopedia, www.investopedia.com, 11 June 2004

allocation of IPOs to officers and directors of public companies, and has already forbidden Citigroup Directors and their families to buy IPO shares³⁵.

The rush on IPO shares in the late 90s was not accompanied by any solid regulation. The aim of privileged investors was to make as much money as possible in as little time as possible. The result of this was that a few years later, when elite investors had made their profits and the real financial situation of many dotcom companies became clear, the dotcom sector largely collapsed, and many normal investors suffered great losses. Appropriate regulations are now slowly put into place. Citigroup now seems committed to help change the whole mindset around IPO allocations. It is expected that they will continue to improve their own policy and cooperate fully with regulatory agencies like the U.S. Securities and Exchange Commission (SEC).

Money laundering

Money laundering is “the process of introducing the proceeds of crime into the legitimate stream of financial commerce in an attempt to mask the origin of the proceeds. The source of the proceeds may include drug trafficking, organized crime, fraud, and many other crimes. Money laundering also provides illicit funds to finance terrorist activities.”³⁶

Citigroup recognises its responsibility to prevent money laundering from happening through its own accounts and customer services. According to the website “no customer relationship is worth compromising our commitment to combating money laundering or the financing of terrorist activities”³⁷. The Group employs more than 300 anti-money laundering Compliance Officers around the world to ensure that the financial system is not misused by criminals or terrorists. Citigroup claims it is an industry leader when it comes to combating money laundering. It works together on the subject with interested parties like the New York Clearing House Association, the Wolfsberg Group, the American Bankers Association and the Financial Services Roundtable.

Some specific anti-money laundering policies of Citigroup are the establishment of a senior-level management position encharged with the matter, the use of an independent monitoring system involving compliance, audit and risk management and legal staff, cooperation with the government on the exchange of terrorist information, adaptation to the new U.S. Patriot Act, and the development of technology that monitors transactions³⁸.

³⁵ Source: Citigroup website, ‘Corporate Citizenship’, IPO Allocations, www.citigroup.com, 2 June 2004

³⁶ Source: Citigroup website, ‘Corporate Citizenship’, Anti Money Laundering, www.citigroup.com, 2 June 2004

³⁷ Source: Citigroup website, ‘Corporate Citizenship’, Anti Money Laundering, www.citigroup.com, 2 June 2004

³⁸ Source: Citigroup website, ‘Corporate Citizenship’, Anti Money Laundering, www.citigroup.com, 2 June 2004

Privacy

Citigroup has its own Privacy Promise for Consumers, a list of ten principles that was published in 1998, and abides by all relevant local privacy laws. In the case these two standards do not coincide, the stricter one applies. Other Citigroup standards include the Code of Conduct, the Information Technology Management Policy, Information Security Standards, the Policy on Confidentiality of Information, and the Corporate Physical Security Standards.

Each consumer business has “named a Privacy Officer to develop, implement, and monitor privacy policies and practices that are appropriate to that business”³⁹. Staff may never give information to third parties, unless through established processes. The 1999 Financial Modernisation Act (or Gramm-Leach-Bliley Act) states new privacy policy requirements for all financial firms. Basically, firms are allowed to formulate their own policy, as long as certain requirements are met and policies are disclosed regularly.

Other industry regulations include the Fair Credit Reporting Act, Regulation E, Model Insurance Privacy Laws and Regulations, and the Right to Financial Privacy Act, as well as certain Internet regulations, marketing regulations and healthcare regulations⁴⁰.

All in all, privacy is one of the best regulated areas of corporate governance for Citigroup. It is also the only area in which no big scandals have led to public indignation in the past few years. Maybe this is a sign that the other areas have been let too loose, especially in the late 90s. This regulation gap is now being filled.

It can be expected that Citigroup will cooperate with authorities on all these corporate governance matters in fear of more reputational damage. On the other hand, Citigroup is well-known for its desire to let the industry regulate itself rather than through local and federal legislation⁴¹. This is probably an important reason behind the many promises of taking an ethical lead in the industry and changing the culture of business ethics within and outside the company. A critical analyst may think that all the time, money and effort Citigroup spends on self-regulation will pay off in the end, if the company is able to convince authorities that binding legislation is unnecessary. In that case, Citigroup will still be free to take advantage of the many loopholes self-regulation leaves open.

1.2.1.2: Corporate Citizenship

As the previous section has pointed out, corporate governance largely refers to *the way* a company is run. Corporate citizenship, on the other hand, has to do with *the kind* of

³⁹ Source: Citigroup website, ‘Corporate Citizenship’, Privacy, www.citigroup.com, 2 June 2004

⁴⁰ Source: Citigroup website, ‘Corporate Citizenship’, Privacy, www.citigroup.com, 2 June 2004

⁴¹ See the sections on lobbying, 1.3.1.8 and 1.3.2.17

activities a company engages in, and the positive contribution it wants to make to society, apart from stimulating economic growth and providing employment. As a minimum rule, good corporate citizenship means that a company does not engage in activities that are harmful to (sectors of) society or to the environment. Both corporate governance and corporate citizenship are part of a company's Corporate Social Responsibility (CSR) policy, since both reflect the ethical choices a company does, or does not, make. Sometimes, the two areas overlap, as in the case of predatory lending, where the unethical practices of insurance salesmen happen to affect one specific -vulnerable- consumer group more than other groups in society. The issue then becomes a social issue as well as a business practices issue.

Citigroup has published a number of documents that describe its corporate citizenship efforts. These include the Corporate Citizenship Report, the Diversity Annual Report, the Foundation Report, the Microfinance report, the Citibank Center for Community Development Enterprise report, the Citibank Community Partners Directory, the California/Nevada Community Commitment and the Annual Report. Most issues are also covered by website summaries. Many NGO's do not consider traditional philanthropy, such as grants to universities and cultural foundations, as an essential part of CSR policy, and therefore the reports and website summaries of such philanthropic activities will not be covered in this report. The other documents and summaries are briefly described below.

The Global Corporate Citizenship Report

The Citizenship Report is the most important corporate citizenship document of Citigroup, and was published for the third time in 2003. The paper focuses on changes and initiatives in four areas of corporate citizenship: affordable housing loans to low- and moderate-income, minority and underserved communities in the U.S.; environmental initiatives; microfinance; and financial education programs. It also covers workplace policies and initiatives and corporate governance issues⁴².

In most CSR areas, the Citizenship Report merely sums up all the initiatives which have been taken or which were continued in the year 2003. Only the environmental chapter includes a general policy description. The other issues are not subject to a company wide policy with rules, guidelines, mission statements, targets, and implementation and monitoring safeguards, but are rather addressed in an ad hoc manner. If there is an overall policy to be discovered in these areas, it is merely 'to promote affordable housing, microfinance, and financial education programs'. The descriptions of the initiatives taken in 2003 are interesting and telling about Citigroup's contribution to society, but too detailed to be mentioned in this SOMO report. For their specific content we therefore refer to the Citizenship Report itself.

⁴² Source: Citigroup website, 'Corporate Citizenship', Corporate Citizenship Report 2003, 2 June 2004

A large section of the Citizenship Report 2003 is devoted to Citigroup's new environmental policy. The year 2003 has marked a turning point for the company in this area, because its environmental policy started from a very weak position and transformed into an example for the entire finance industry. In this section, we will only focus on the structure of Citigroup's environmental policy and on some examples of recent initiatives in this area, whereas the specific changes in environmental commitments will be further discussed in section 1.2.3.

Citigroup has an Environmental Management System, which is said to be part of its 'core business practice'. The EMS was updated in 2003 and now consists of nine sections⁴³:

1. External listening
2. Internal policy
3. Organisation and people
4. 'Our environmental footprint'
5. Training and communications
6. Risk management
7. NGO partnerships
8. Businesses making a difference
9. Evaluation and future planning

1. External listening

Citigroup wants to make clear that it takes its stakeholders seriously by putting stakeholder dialogue first in its EMS. The Global Community Relations office carries the principal responsibility for engaging in stakeholder dialogue on environmental issues.

Before Citigroup came into being in 1998, some of its current components had already signed the UNEP Statement by Financial Institutions on Environment and Sustainable Development⁴⁴. This statement has been the basis for many aspects of Citigroup's environmental policy. Citigroup is on the steering committee of UNEP-FI⁴⁵ Financial Institutions Initiative, and has participated in the 2003 UNEP-FI Global Roundtable Meeting on Finance and the Environment⁴⁶.

Citigroup's environmentally aware shareholders have formed a Shareholder Dialogue Group a few years ago, together with two NGO's. The Group also discussed social policies, practices and performance. Citigroup says it is open to criticisms from this Group. Also, Citigroup says it has engaged in an extensive dialogue with the Rainforest Action Network,

⁴³ Source: Citigroup website, 'Corporate Citizenship', Corporate Citizenship Report 2003, 2 June 2004

⁴⁴ See Annex 1

⁴⁵ UNEP-FI = United Nations Environment Programme Finance Initiative

⁴⁶ Source: UNEP-FI website, <http://unepfi.net/fii/index.htm>, 12 June 2004

a Californian NGO which has campaigned against Citigroup for four years, since the beginning of 2000.

Citigroup was one of the ten banks who developed the Equator Principles⁴⁷ and signed them in June 2003. Since then, 15 other banks have signed this document as well. The Equator Principles are designed to regulate project finance for projects larger than \$50 million dollars. The Principles require that signatory banks first assure that a project has no unacceptable environmentally and socially harmful effects, before they provide capital to the project. Equator banks are committed to a screening process based on the guidelines of the International Finance Corporation (IFC)⁴⁸. The screening applies to all sectors of industry, including mining, oil, gas and forestry⁴⁹.

More specifically, the Equator Principles require the potential borrower to demonstrate that the project complies with the World Bank Pollution and Abatement Guidelines. If the borrower operates in a low- or middle-income country, the company doing the project also has to report on its compliance with the IFC's Safeguard Policies. One of the weaknesses of the Principles that have been pointed out by NGO's is, that adherence to the Equator Principles is completely voluntary for signatories, and cannot be externally enforced⁵⁰.

2. Internal Policy

The major changes in Citigroup's internal environmental policy over the past year have been the adoption of the Equator Principles in June 2003 and the adoption of the Environmental and Social Risk Management Policy by the Global Corporate and Investment Banking (GCIB) Group in October 2003. This new policy was made known to the public in January 2004 and is further described in section 1.2.3.

3. Organisation and people

High level management meets at least once a year to talk about environmental issues. The people involved are the Public Affairs Committee, the Senior Vice President of Global Community Relations, the Environmental Affairs unit and management and staff members. The Environmental Affairs unit is responsible for information flows, external relations, policy development and reporting. Citigroup also has an Environmental and Social Policy Review Committee which consists of senior managers from various parts of the company. For a full picture of who is doing what in Citigroup to improve environmental policy,

⁴⁷ See Annex 2

⁴⁸ The IFC is the private-sector investment arm of the World Bank

⁴⁹ Source: Equator Principles website, www.equator-principles.com, 12 June 2004

⁵⁰ Source: The collective NGO analysis of the Equator Principles, Rainforest Action Network website, http://www.ran.org/news/equator_ngo.html, 12 June 2004

practices and performance, the following table has been copied from the Citizenship Report⁵¹:

Environmental Responsibility		
ORGANIZATION	STAFFING	RESPONSIBILITY
Environmental and Social Policy Review Committee	Eight to ten Senior Managers representing the Global Corporate & Investment Banking Group, Legal, Corporate Governance, and Risk Management	Consults on policy and environmental issues
Environmental Affairs	Four to five individuals led by Senior Vice President	Advises on environmental policy development, provides expertise to line businesses, manages NGO relationships, advises on grants
GCIB Credit Risk	More than 20 Senior Credit Officers supported by Environmental Risk Management Director	Responsible for implementing new environmental and risk management policy
Board of Directors	Public Affairs Committee	Briefed annually on company status, initiatives, policies and issues
Investment Group	Investment Committee for Sustainable Forestry and Renewable Energy Program	Responsible for making investments
Project Finance	Entire professional staff	Responsible for implementing Equator Principles
Consumer Bank	CitiMortgage sales and marketing representatives	Market a Fannie Mae environmental mortgage product
Consumer Bank	More than 50 Community Development lending directors and relationship managers	Identify brownfields community development financing opportunities and finance LMI housing projects
Corporate Real Estate Services	150 Facilities Managers	Responsible for reducing environmental footprint
Public Finance	More than 14 senior environmental bankers; more than ten senior housing bankers	Responsible for financing water, sewerage, solid waste, recycling and brownfields projects as well as low-income housing projects
Purchasing	Seven purchasing professionals	Identify environmentally preferable products and services, and communicate Citigroup's environmental commitment to our suppliers

4. 'Our environmental footprint'

Citigroup launched its own environmental database and an energy management website in 2002. Through a survey, Citigroup's overall consumption of electricity, water, gas, paper and other commodities was measured for the years 2000, 2001 and 2002. In 2003, Citigroup

⁵¹ Source: Citigroup website, 'Corporate Citizenship', Corporate Citizenship Report 2003, p. 33. 2 June 2004

worked on further standardising the research process and educating its staff in using the energy management website. Citigroup realised that its energy consumption data for the previous years had been incomplete and took measures to improve the accuracy of the results produced by the survey. The company is now working to check its 2003 numbers, which will eventually serve as a baseline for comparing future figures.

In 2003, Citigroup published three reports on the results of the internal consumption and emissions survey: the Global Consumption Report, the Global Consumption Emissions Report and the 2003 Environmental Projects Initiated report. The first two reports reflect and interpret the data found in the survey, whereas the third report lists the consumption reduction projects that were started around the world.

At Citigroup, an Energy Allocation/ Awareness Program has been started with which facility managers and operators can monitor and reduce the energy consumption of the office under their control. Daily and monthly consumption targets are set, against which actual levels are compared. In 2003, the company joined the BRT Project 'Climate Resolve', in which a group of U.S. companies voluntarily commits itself to the reduction of greenhouse gas emissions. Citigroup is also a participant in the 'Climate Northeast' forum on greenhouse gas issues.

Citigroup engaged in a partnership with the Alliance for Environmental Innovation (a project of Environmental Defence), to change its policy on copy paper. In 2003, the company switched to recycled paper instead of virgin paper for all its U.S. offices. Also, paper suppliers are from now annually tested on their environmental practices, employees are discouraged from using too much paper and documents are increasingly made available online. All in all, paper use declined from 116 million sheets to 40 million sheets in the course of one year. Citigroup organised a workshop for other companies on paper use in November 2003.

5. Training and communications

In 2003, 1,500 employees were trained on the new environmental policies of Citigroup, including the Equator Principles and the new GCIB Environmental and Social Risk Policy. Training took place in all regions, except Latin America and the Asia-Pacific region, where bankers and risk managers will be trained in 2004.

Furthermore, efforts were made to communicate Citigroup's new policies to shareholders, employees and other stakeholders, mainly through the internet.

6. Risk management

The environmental and social risk assessment of projects financed by Citigroup is modelled after the risk assessment procedures of the Equator Principles. Projects that fall under the scope of the Principles are categorised as A, B or C projects, referring to high, medium or

low environmental and social risk. For projects that fall in the A or B categories, the borrower has to supply Citigroup with an Environmental Assessment paper which describes the risks and how they will be handled by the borrower.

Under the new GCIB Environmental and Social Risk Management Policy, the same risk assessment procedure is used, but it is applied to more projects, including all projects that are funded through loans and bonds, *where the use of proceeds is known*. The GCIB policy focuses on category A projects, but the evaluation is stricter than under the Equator Principles. The capacity of the borrower to manage social and environmental risks is judged by Citigroup and internal special approval must be obtained before any transaction occurs.

The social issues that fall under the risk assessment procedures laid out in the Equator Principles and the GCIB Environmental and Social Risk Management Policy are only those issues which are directly related to the projects to be funded. Indigenous rights and stakeholder consultation, for instance, fall under Citigroup's project management policies. More general social issues such as consumer rights and most labour rights, for instance, do not fall under the Equator Principles or the GCIB policy⁵².

Citigroup, like all other financial firms, makes a difference between direct or indirect involvement in a client's activities: it only takes responsibility for its clients' actions if these are undertaken directly with the help of the bank. So when Citigroup grants a loan for the construction of a dam, for example, it is co-responsible for the environmental and social consequences of that dam. But if it provides a loan to an institution which constructs a controversial dam, but also other infrastructural projects, and the loan does not directly go to the financing of the dam, then the bank is not responsible for the consequences of the dam project.

This was the case with Citigroup's involvement with the China Development Bank in 1999. CDB was constructing the Three Gorges Dam in China that caused great environmental damage and the dislocation of over one million people. But when underwriting the bond offering for CDB, Citigroup was assured that the proceeds would not be used to finance the dam. Technically, Citigroup was therefore not directly involved with the project and carried no responsibility for its consequences⁵³.

7. NGO partnerships

Citigroup maintains several partnerships with environmental NGOs. The goal of the partnerships is to exchange information, and work together on the realisation of projects

⁵² Only occupational health and safety are included in the provisions of the two commitments.

⁵³ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

regarding sustainable development. The main areas of interest to Citigroup are the loss of biodiversity and the social impacts of deforestation and climate change.

The partnerships that are described in the Citizenship Report are:

Partner	Goal	Type of project	When	Where
Conservation International (CI)	Conserving biodiversity	Environmentally sound agriculture	Since 1996	Brazil, Peru, South Africa
E+Co	Promoting clean energy	Help small and medium sized clean energy projects to use carbon trading as a source of finance	2003	Latin America
Forest Trends (FT)	Protect forest ecosystems	Developing and promoting sustainable forestry products	2003	Mexico
The Nature Conservancy	Promoting clean energy and forest protection	Replacing wood for fuel by clean energy sources	2003	China
Rainforest Alliance	Encouraging sustainable coffee and cocoa farming	Assisting in production and promotion of eco-cocoa and specialty coffee	2003	Ecuador, El Salvador
World Resources Institute	Sustainable enterprise development	Financial and technical assistance to small and medium sustainable enterprises	2003	China

8. Businesses making a difference

Citigroup is seeking sustainable business opportunities and has come up with two new initiatives in this area in 2003. The first concerns a program to identify investment opportunities in the sustainable forestry and energy sectors, and the second is the participation in a fund that redevelops so called brownfield sites.

Apart from these initiatives, Citigroup continued to provide funds for sustainable projects in 2003, financing 158 projects worth \$8.3 billion during the course of the year⁵⁴. Projects included pollution control, water and sewerage, recycling and solid waste disposal facilities, and energy efficient projects. Also, in the Phillipines, Citibank arranged a loan to the food, beverage and packaging giant San Miguel, with the intention to establish a recycling program for plastic (PET) bottles.

Some of the projects that Citigroup includes in its ‘sustainable business’ category, may not be regarded as such by environmental and social groups with higher standards. For instance, a number of power projects in Brazil are considered sustainable by Citigroup because they include environmental and social programs, but it is not unthinkable that the local population and NGO’s see many more negative aspects of these projects than positive ones, and therefore do not qualify these power plants as sustainable businesses.

9. Evaluation and future planning

⁵⁴ Source: Citigroup website, ‘Corporate Citizenship’, Corporate Citizenship Report 2003, p. 43, 2 June 2004

In this last section, Citigroup comments on its progress and makes promises of future improvements of its environmental policy.

Finally, throughout the environmental section of the Citizenship Report, a number of issues in which Citigroup takes a special interest are brought to the attention. One of them is climate change. The Group says it is “taking a proactive stance on this important issue by reducing greenhouse gas emissions from its own operations, assisting customers in developing financial solutions to help reduce emissions and investing in renewable energy”⁵⁵. Citigroup also wants to publish a carbon intensity index on any new power generating projects it finances. Climate friendly investments so far focus on renewable energy sources and residential clean energy financing.

For the Citizenship Report as a whole, the GRI (Global Reporting Initiative) and OECD guidelines on sustainability reporting were used. However, not all indicators of these guidelines are covered in the report. At the end of the report, a list is provided which identifies the specific reporting guidelines that have been covered.

Microfinance report

The Citigroup Microfinance report was published in 2002 to cover the microfinance initiatives that were running throughout the world at that moment. The report has not been updated since, but since most partnerships with microfinance institutions (MFIs) are concluded for several years, and new partnerships are covered in the Citizenship Report, it is possible to get a good idea of the programs Citigroup is currently engaged in.

Generally speaking, Citigroup’s efforts in the microfinance realm focus on technical assistance, institution building and the capitalisation of loan funds. But more recently, the Group has also started to give letters of credit to MFIs, and to help them issue bonds. These recent trends indicate that Citigroup is increasingly recognising MFIs as fully-pledged business partners.

Diversity Annual Report

From a Corporate Social Responsibility perspective, Citigroup’s efforts to diversify its workforce are not so interesting. Workforce diversity is usually not regarded as a CSR issue. Therefore, the Diversity Report will not be treated here.

Citibank Center for Community Development Enterprise report

⁵⁵ Source: Citigroup website, ‘Corporate Citizenship’, Corporate Citizenship Report 2003, p. 42. 2 June 2004

The 2002 'CCDE report' provides information on Citigroup's involvement in community development (or: housing) projects. Citibank's CCDE strives to make affordable housing initiatives available to elderly people, minorities and universities, amongst others. To achieve this, Citibank arranges financing packages for non-profit and for-profit developers that operate in low- and middle- income areas. Citibank's CCDE works together with Salomon Smith Barney, CitiMortgage, Travelers and the Citigroup Foundation in financing community development.

CCDE operates in 11 U.S. states, and offers lending and investment services such as letters of credit, construction loans, mortgages, and low-income housing tax credit investments to developers. For the specific initiatives Citigroup has taken in this area, we refer to the CCDE report, which is available on Citigroup's website (www.citigroup.com).

Annual Report

The Annual Report 2003, in its 'global community' section, sums up the changes and improvements to Citigroup's corporate citizenship policies and practices over the last year. The report quickly refers to the four key CSR areas Citigroup focuses its efforts on: education, environment, microfinance and investing in LMI communities. Just as in the area of corporate governance, the Annual Report also provides very little information about corporate citizenship.

Company website

Citigroup's website covers the following corporate citizenship issues:

1. Social responsibility
2. Microfinance
3. Environment
4. Diversity
5. Community relations
6. Financial education
7. Child care
8. Philanthropy
9. Welfare-to-work

The website gives a good overview of Citigroup's policies and activities in these areas. Most of these activities, however, are not regarded as part of CSR policy by the international NGO community. The areas which are important, such as Citigroup's environmental policy and microfinance initiatives, have already been treated above.

A final note on Citigroup's corporate citizenship policy is that the Group is member of the following business associations for sustainability:

- BSR: Business for Social Responsibility is a global non-profit organisation that promotes Corporate Social Responsibility through providing information, advisory services and discussion to member corporations. BSR was founded in 1992⁵⁶.
- EBA: the Environmental Bankers Association was established in 1994 as a non-profit trade association representing the financial industry. The EBA focuses on environmental risk management⁵⁷.
- WEC: the World Environment Center has been promoting sustainable development for over 30 years⁵⁸.
- UNEP-FI: United Nations Environment Programme Finance Initiative. Citigroup is an active member of UNEP-FI, being one of five members of the North American task force⁵⁹.

1.2.2: New elements in Citigroup's CSR policy

1.2.2.1: Corporate governance

The most important changes in Citigroup's corporate governance policy are explained in a document called the Citigroup Initiatives Corporate Governance Business Practices report, which was published in the spring of 2003.

This Initiatives report outlines the measures that were taken after some financial scandals and several lawsuits had badly damaged Citigroup's reputation in 2002. From these events it became clear that new standards were needed to regulate behaviour in the areas of research and investment banking (conflict of interest), IPO share allocation practices (favouritism), structured finance (hiding of clients' company losses) and transparency. The measures were intended, according to Citigroup, to restore consumer confidence and to establish a renewed ethical leadership in the financial sector.

The new enhanced corporate governance policies have to ensure that "the way [Citigroup does] business not only leads the industry but satisfies basic, common-sense standards for integrity and long-term market interests"⁶⁰ (which seems to imply that satisfying basic standards is a greater challenge than taking industry leadership!). Among the policy changes in 2002-2003 are:

- The creation of Business Practices Committees in every Citigroup business unit and at the corporate level that review ethical questions regarding products and practices;

⁵⁶ Source: BSR website, www.bsr.org, 17 June 2004

⁵⁷ Source: EBA website, www.envirobank.org, 17 June 2004

⁵⁸ Source: WEC website, www.wec.org, 17 June 2004

⁵⁹ Source: UNEP-FI website, www.unepfi.net, 17 June 2004

⁶⁰ Source: Citigroup website, 'Corporate Citizenship', Citigroup Initiatives: Spring 2003, p. 2. www.citigroup.com, 2 June 2004

- The creation of a new research division, Smith Barney;
- Restrictions on analysts' interaction with bankers;
- Creation of the U.S. Equity Research Policy Committee;
- Citigroup Directors may no longer buy IPO shares;
- Structured finance transactions may only occur if the client discloses the net effect of the transaction in its financial statements;
- Updating the Code of Conduct and requiring every employee to read and sign the renewed version;
- Adjustments to financial reporting practices to increase transparency, for instance by sticking to GAAP income measures only.

The details about these and other changes in corporate governance polices can be found in the Initiatives report.

1.2.2.2: Corporate citizenship

The most important recent change regarding corporate citizenship has been the adoption of the Global Corporate and Investment Banking group's (GCIB) Environmental and Social Policy in 2003.

Citigroup's new environmental policy is basically a reflection of the Equator Principles which Citigroup signed on June 4, 2003. The Equator Principles, based on the World Bank's IFC guidelines, commit banks to assess the environmental and social impact and safeguards of any large projects which they finance. However, many NGO's feel that the Equator Principles do not offer enough protection to the environment and to local populations because of some critical fallacies in the document, which are:

1. The scope of the Equator Principles is too limited, for instance: there is no reference to categorical prohibitions. This means even destructive practices in sensitive areas may get funding if safeguard measures look good on paper.
2. The Principles only apply to project finance while many destructive industries, like mining and forestry, are usually financed through other mechanisms.
3. The Principles offer no guarantee of actual implementation.
4. The Principles do not require signatory banks to disclose relevant information about financing decisions. The lack of transparency makes it hard for outsiders to verify if banks are living up to their new standards.
5. The Principles rather consist of vague promises than of clear commitments.
6. The Principles are weak on social issues and do not adequately guarantee the respect of human rights.
7. NGO's fear that the Principles may reduce incentives for banks to develop and/or adopt other, stricter standards.
8. Under the Equator Principles, the *borrower* is responsible for supplying all the information and meeting all the environmental and social requirements, while the

lender carries very little responsibility for the planning and the effects of the project. In the case of non-compliance with the Principles, the affected communities cannot hold the banks accountable⁶¹.

Citigroup's environmental policy had been the target of public protest for years, and even after the Group adopted the Equator Principles, the NGO community, led by the Rainforest Action Network, continued its campaigns against the company. The ongoing pressure paid off in January 2004, when Citigroup announced its own, new environmental policy, which goes beyond the Equator Principles on a number of points⁶².

The new Environmental and Social Risk Management Policy of the Global Corporate and Investment Banking (GCIB) Group is still based on the Equator Principles, but includes specific sections on high-caution zones, illegal logging, investing in sustainable development, and climate change. The policy includes a categorical exclusion for the financing of commercial logging activities in primary rainforests, for non-sustainable extractive activities in forests of high ecological value, and for the destructive expansion of plantations. Also, the policy commits Citigroup to a proactive stance towards combating illegal logging, and to promoting sustainable development. Citigroup promises to take positive action in three areas, namely investing in sustainable logging, in renewable energy and in clean and efficient residential energy. Finally, Citigroup announces its new reporting efforts in the area of greenhouse gas emissions, which cover 1) internal energy use and 2) the greenhouse gas effects of the power projects in its own portfolio. Results will be published annually in the Corporate Citizenship report.

With the publication of the GCIB Environmental and Social Risk Management Policy, Citigroup instantly became the global financial sector leader in the field of environmental responsibility, a position that had been occupied by the Dutch ABN-Amro bank since 2001. ABN-Amro had been applauded for years because of its commitment to the preservation of old-growth forests. Citigroup had been challenged by NGO's to 'meet or beat' ABN-Amro's environmental policy, and ended up beating it. Citigroup is the first, and so far the only, financial firm to "prohibit investment in any extractive industry in primary tropical forests and place severe restrictions on destructive investment in all endangered ecosystems worldwide"⁶³. Citigroup also is the first firm with an illegal logging policy requiring all legal documents and permits before closing a financing deal and the first to monitor its impact on climate change and committing to invest in renewable energy.

Strangely enough, at the time of writing (June 2004), the new policy as quoted in annex 3 below can no longer be found on Citigroup's own website, where it previously could be

⁶¹ Source: The collective NGO analysis of the Equator Principles, Rainforest Action Network website, http://www.ran.org/news/equator_ngo.html, 12 June 2004

⁶² See Annex 3

⁶³ Source: RAN website, http://www.ran.org/ran_campaigns/global_finance/citi_victory.html, 28 May 2004

found under www.citigroup.com/citigroup/environment/data/initiatives.htm. It is unclear whether the page has been removed temporarily or permanently.

1.2.3: Citigroup’s CSR commitments

The sections above show that there are, in total, three sets of specific CSR commitments to which Citigroup is bound, even though they all ultimately rely on voluntary adherence (except for some corporate governance aspects of the Code of Conduct which can be legally enforced, like basic transparency initiatives and money-laundering policies). The three commitments of Citigroup, which are all printed in the annexes to this report, are:

	Corporate governance	Corporate citizenship
1	The Code of Conduct	
2		The Equator Principles
3		The GCIB Environmental and Social Risk Management Policy

1.3: Citigroup and controversial CSR issues

Citigroup has been one of the most controversial financial companies of the late 90s and early 2000s. Many of Citigroup’s activities have been the subject of heated public debate in the national media in the U.S. and of large scale campaigns by U.S. based NGO’s. Consequently, there is a lot of information available on Citigroup’s (alleged) malpractices, on the legal cases that were brought against the Group, on the settlements it agreed to pay and on the changes in CSR policies the company made to avoid future criticism. Below is a list of issues that were raised over the last four to five years concerning Citigroup’s CSR behaviour, including a short description of each issue and, where applicable, the way Citigroup has tried to solve the problem.

1.3.1: Corporate governance issues

Wall Street investigations

The most well-known financial scandal Citigroup played a lead role in was the Wall Street research and IPO allocation scandal that was brought to the light in 2001, when New York State Attorney General Eliot Spitzer started investigating possible conflicts of interest between the research and investment banking activities of financial firms. In the case of Citigroup, it was found that Salomon Smith Barney (now called Citigroup Global Markets) was guilty of the following malpractices:

- There was no good policy to manage conflicts of interest between research and investment banking divisions;
- Salomon Smith Barney (SSB) published misleading research on internet- and telecommunications companies, which overstated their potential, and thus benefited

these companies (which were also investment banking clients) and SSB itself, while harming investors who based their investment decisions on fraudulent research.

- SSB failed to address the problem even though internal e-mails revealed that several people knew about analyst's misleading research practices.
- SSB was also involved in unfair allocation of IPO (Initial Public Offering) shares through spinning and laddering practices.

Spinning and laddering are unethical, but not necessarily illegal, financial practices that have to do with the sale of Initial Public Offering (IPO) shares. Spinning refers to the practice of investment brokerage houses of selling IPO shares to top executives of companies in return for business. Laddering means that investment brokers artificially drive up the prices of IPO shares, hoping to please the company issuing the IPO, and therefore to obtain more IPO underwriting business from that company⁶⁴.

In April 2003, Citigroup agreed to pay a fine of \$400 million, and to take appropriate measures to deal with the problem of conflicts of interest. One of SSB's former star analysts, Jack Grubman, was banned from the investment broker profession altogether and had to pay an additional \$15 million from his own pocket⁶⁵.

One year later, in May 2004, Citigroup settled charges with purchasers of WorldCom securities for a total amount of \$2.65 billion dollars. Investors felt they were lured into buying WorldCom stocks through the positive ratings by SSB analysts, especially Jack Grubman. In reality, the WorldCom hype turned out to be a bubble, that burst in 2002 when the company went bankrupt after its massive accounting fraud was brought to the light. The price of WorldCom shares immediately dropped to a third of their original value and investors lost millions of dollars.

Although Citigroup denied that it had been engaged in any illegal activity, it agreed to pay compensation to people who had invested in WorldCom between April 1999 and June 2002⁶⁶. It became clear from the investigations that Jack Grubman, who was close friends with WorldCom's CEO Bernard Ebbers, was co-responsible for hyping WorldCom shares, and that SSB had allocated hot IPO shares to WorldCom executives. Ebbers alone made a \$11.5

⁶⁴ Source: online investment encyclopedia, www.investopedia.com, 23 June 2004

⁶⁵ Sources: U.S. Securities and Exchange Commission, Litigation Release No. 18111 / April 28, 2003. <http://www.sec.gov/litigation/litreleases/lr18111.htm>, 2 June 2004; Salomon Smith Barney, Citigroup Settlement Terms, Edgar Snyder website, http://www.edgarsnyder.com/securities_fraud/salomon_smith_barney.html, 2 June 2004; Zakenbanken op strafbank, <http://www.veb.net/effect/effectartikel.php?newsnr=211&SID=7bd0e57eb5241581a6c4928be2688935>, 10 June 2004; CONFLICT PROBES RESOLVED AT CITIGROUP AND MORGAN-STANLEY, April 28, 2003, http://www.oag.state.ny.us/press/2003/apr/apr28a_03.html, 2 June 2004

⁶⁶ Source: AFX News Limited, Citigroup Reaches \$1.6B Settlement on WorldCom Suit, May 28, 2004. <http://www.ecommercetimes.com/story/33708.html>, 2 June 2004

million dollar profit from his IPO shares, and in return gave 23 banking investment assignments to SSB that earned the bank \$107 million in commission fees⁶⁷.

Strangely enough, Citigroup's then CEO Sandy Weill did not have to make any personal sacrifices after the investigations of Wall Street scandals, although he was personally involved in Citigroup's conflicts of interest problems. For instance, he urged Jack Grubman to give a positive rating of the company AT&T, where his friend and Citigroup Board Member Michael Armstrong was CEO. In return, Weill would help Grubman get his children into an exclusive New York pre-school.

All in all, the fines that Citigroup had to pay, and will have to pay for future lawsuits regarding the Wall Street malpractices of the late 90s and early 2000s, are small compared to the profits Citigroup made during the years of the internet and telecommunications hype⁶⁸. In the meantime, Citigroup has made the required adjustments to its internal policy on possible conflicts of interest, as described in section 1.2.1.1.

Mutual funds abuses

A mutual fund basically is a collection of stocks, bonds and other securities that is put together by a bank on behalf of a large number of small investors. Investors buy shares of a mutual fund, and thus become co-owner of a diverse investment portfolio. The major benefits of mutual funds are that the investor does not have to manage the portfolio himself but lets professional investment bankers manage it for him, and that the risk of the mutual fund is spread because a mutual fund portfolio typically contains many different companies. Some downsides of mutual funds are that the shareholders have little control over the portfolio, that they pay fees to the fund manager, and that returns are usually not very high.

As to the fees fund managers charge for their services, these fees can take many different forms, and it is often hard for investors to get a good oversight of the costs of their transactions and other fund management services. It is also hard for investors to compare the fees different funds charge, and thus make an informed choice about the fund they choose to invest in. Sometimes, fund fees can cause indignation among investors that feel they are confronted with unexpectedly high costs. For example, in December 2003, Citigroup Asset Management agreed to refund \$16 million to mutual fund investors who were overcharged for stock transactions.

⁶⁷ Source: Zakenbanken op strafbank,
<http://www.veb.net/effect/effectartikel.php?newsnr=211&SID=7bd0e57eb5241581a6c4928be2688935>, 10 June 2004

⁶⁸ Sources: Citigroup to Pay \$2.65B to Settle Case, May 10, 2004. <http://www.wjla.com/headlines/0504/145717.html>, 2 June 2004; Deny, Deny, Deny, \$2.65 Billion, May 11, 2004. http://www.forbes.com/business/2004/05/11/cx_da_0511topnews.html, 2 June 2004

There have been some additional problems with mutual funds that stem from improper practices by fund managers. Again it was New York State Attorney General Eliot Spitzer who turned America's attention to mutual funds abuses. Two frequently occurring controversial activities he investigated were market timing and late trading. Market timing means that an investment manager tries to predict short term movements in the market or in specific sectors and adjusts his portfolio accordingly, for instance by switching between sectors or between stocks and bonds⁶⁹. Most mutual funds prohibit this practice because it is more risky than a passive portfolio, and there are usually no gains for shareholder in the long run. Market timing can be considered fraud if investors are not made aware that the fund allows this kind of practice⁷⁰.

Late trading occurs when special investors like hedge funds are allowed by the mutual fund to buy or sell shares after the market has closed at 4 p.m., but still at that day's prices, while it might already be clear from the news what the prices are likely to do the next day. Thus, the next morning the shares are sold or bought again as the market opens, and the privileged investor can walk away with the profits⁷¹.

A similar privilege is given to special investors when they are allowed 'rapid trading', while other investors are bound to procedures that limit frequent transactions. But mutual fund abuse doesn't end here. In this industry too, a big problem exists regarding conflicts of interest between brokerage firms and mutual fund managers. There are all kinds of possible agreements between a company's brokerage and mutual fund branches, where mutual funds promise commission fees or other advantages to brokerage firms if these promote the mutual fund's shares to their customers⁷².

Another conflict of interest problem is that investment banks may want to please their client companies by holding their shares in mutual funds, even when the client company is not an attractive investment opportunity. The Securities and Exchange Commission showed that in 2002, Citigroup banking clients also made up more than 30% of mutual fund shares, while independent fund managers showed much less interest in buying shares in these specific companies. This is a serious abuse, since fund managers who privilege client company shares do not fulfil their duty of maximizing returns for investors, but rather choose to maximise their investment bank's profits⁷³.

⁶⁹ Quick MBA Finance, Market timing, <http://www.quickmba.com/finance/invest/timing/>, 23 June 2004

⁷⁰ Citigroup after the merger, January 2004, http://www.uow.edu.au/arts/sts/bmartin/dissent/documents/health/Citigrp_after98#Fraud%20by%20employees

⁷¹ MSNBC New Services, "Spitzer wants funds to cut fees", 2 December 2003, <http://msnbc.msn.com/id/3606432/>, 10 June 2004

⁷² Source: Socially Responsible Investment Media, "U.S. mutual fund industry reform bill announced in Washington", 9 February 2004, http://www.srimedia.com/artman/publish/article_747.shtml

⁷³ Source: Citigroup Uses Mutual Funds as 'Dumping Grounds' for Clients, Bloomberg, April 29, 2004. <http://quote.bloomberg.com/apps/news?pid=nifea&sid=adTuc7JN6Bvw>, 10 June 2004

The abuses in the mutual fund industry - high fees, market timing, late trading, rapid trading and the dumping of banking clients' shares in mutual funds - were all very common in the late 90s and early 2000s in the U.S., because regulation on the mutual fund industry was weak (in part because of strong lobbying efforts by allfinanz businesses like Citigroup). After Spitzer's investigations, however, banks and mutual funds did everything they could to prove they could regulate their own behaviour, promising to eliminate abuses and to focus again on investors' interests. In February 2004 the Mutual Fund Reform Act was announced by the U.S. Senate to stress the importance of reform in the areas of fund fee transparency and conflicts of interest⁷⁴. It is expected that Citigroup will make the necessary changes to its policy and report on these in the Corporate Citizenship Report 2004.

Hiding company debts

Citigroup has been involved with various structured finance scandals over the last few years. In these cases, Citigroup client companies have used structured finance arrangements to hide their debt, thereby fooling investors and the public about their real financial situation. The most well-known case has been the American energy company Enron, which went bankrupt in 2001. After investigations by the Securities and Exchange Commission, Citigroup agreed to settle in July 2003 and paid over \$100 million in disgorgement, penalties and interest for its structured finance work for Enron. Citigroup did not deny nor admit any wrongdoing or liability. In the end, the transactions made by Citigroup may have been legal, but were generally regarded as unethical, which was why Citigroup did not protest against the penalties imposed⁷⁵.

Another world famous accounting scandal related to Citigroup is the case of Parmalat. Citigroup is currently under investigation for its involvement with the Italian dairy company, which was declared bankrupt on December 27, 2003, after a 10 to 13 billion euro accounting fraud was exposed. Citigroup has provided all sorts of financial services to Parmalat during the last 15 years, including loans, bond issues, merger & acquisitions advice and currency services. As one of the biggest lenders to the Italian company, Citigroup has been appointed as the main representative of more than 25 international lenders to Parmalat. Although most of the transactions Citigroup engaged in were legal, one Citigroup subsidiary called Buconero - which means 'black hole' in Italian - arranged structured finance deals for Parmalat, and helped the company book its debt as equity⁷⁶.

⁷⁴ Source: Socially Responsible Investment Media, "U.S. mutual fund industry reform bill announced in Washington", 9 February 2004, http://www.srimedia.com/artman/publish/article_747.shtml

⁷⁵ Sources: Citigroup statement, July 28, 2003, <http://www.citigroup.com/citigroup/citizen/structuredfinance/030728a.htm>, 23 June 2004; SEC press release, July 28 2003, <http://www.sec.gov/news/press/2003-87.htm>, 23 June 2004

⁷⁶ Sources: Financial Times, Citigroup gives details of 15-year association, 19 January 2004; Citigroup after the Merger, http://www.uow.edu.au/arts/sts/bmartin/dissent/documents/health/Citigrp_after98#Fraud%20by%20employees, 2 June 2004

Other, less known examples of dubious structured finance accounting practices by Citigroup involved the companies Dynegy and Adelphia Communications, and various companies in Japan, where the Japanese branch of Citibank was penalised by Japan's financial services agency for illegally helping clients to conceal losses in 2001⁷⁷. Structured finance deals were also an issue in the Citigroup - WorldCom case.

In 2002 Citigroup introduced its 'net effect' rule to assure that similar involvement in accounting fraud would not occur again in the future.

Money laundering

Over the years, Citigroup has been accused of helping many influential people worldwide to launder their money through Citigroup bank accounts. Some of the people that have damaged Citigroup's reputation in this area in the period of 1994 until 2002 are Sani Abacha (former president of Nigeria), Mohamad Atta (9/11 terrorist), Omar Bongo (president of Gabon), Jaime Lusinchi (former president of Venezuela), Paulo Maluf (former mayor of Sao Paulo), Carlos Menem (former president of Argentina), Raoul Salinas (brother of the former president of Mexico), Suharto's daughters (former president of Indonesia), Asif Ali Zardasi (husband of former prime minister of Pakistan Benazir Bhutto), and Jorge Zorreguieta (former minister of agriculture in Argentina)⁷⁸.

Citigroup has also been heavily criticised for its acquisition of Banamex in 2001, because the Mexican bank was known to be involved in large scale money laundering practices. Banamex owner Roberto Hernandez was proven to be personally connected to a cocaine smuggling network, but was still allowed to join the Citibank Board. A few years earlier, in 1999, then U.S. Treasury Secretary Robert Rubin, who is now Chair of Citigroup's Executive Committee, led 'Operation Casablanca', which was meant to combat Mexican money laundering by Banamex and other Mexican banks. One inside informant later accused Rubin from shutting down the investigation before connections with U.S. banks were exposed⁷⁹.

Citigroup, as explained in section 1.2.1.1, has an anti-money laundering policy in place and employs more than 300 Anti-Money Laundering Compliance Officers worldwide, who have to make sure all applicable laws are respected. The policy is regularly updated, and to

⁷⁷ Sources: Citigroup after the Merger, http://www.uow.edu.au/arts/sts/bmartin/dissent/documents/health/Citigrp_after98#Fraud%20by%20employees, 2 June 2004; <http://www.centralbanking.co.uk/newsmakers/archive/2001/aug22.htm#News07>, 23 June 2004; http://money.cnn.com/2002/05/31/news/companies/citigroup_dynegy/, 23 June 2004, Executive Intelligence Review, The Story Behind Parmalat's Bankruptcy, 16 January 2004, http://www.larouchepub.com/other/2004/3102parmalat_invest.html, 23 June 2004

⁷⁸ Sources: Transnationale website, www.transnationale.org, 4 July 2003; de Groene Amsterdammer, 'De B.V. Zorreguieta', 16 March 2002

⁷⁹ Source: Rainforest Action Network website, Citigroup becomes Mexico's largest bank after Banamex merger, 10 August 2001, www.ran.org, 28 May 2004

date no instances of money laundering have been found for the years 2003 and 2004. In October 2003 Citigroup Tanzania hosted an Anti-Money Laundering Training Workshops in Dar es Salaam, showing the Group's commitment to combating money laundering practices in the financial industry⁸⁰.

Lobbying: market access and financial regulation

Citigroup has been famous for its lobbying activities ever since the financial firm came into being with the merger of Citicorp and Travelers in 1998. The merger itself was technically illegal at the time since the 1933 Glass-Steagall Act prohibited commercial banking and investment banking activities to take place under one roof because of the possible conflict of interest. But president Clinton and Alan Greenspan gave Citigroup a temporary dispensation from the Glass-Steagall Act to allow the merger, and by 1999 extensive lobbying from the part of Citigroup had ensured that the law was repealed, making allfinanz businesses possible.

Under Sandy Weill's supervision, Citigroup pushed for new legislation and ended up having a great influence on the creation of a new law, the Gramm-Leach-Bliley Act, also known under the name Financial Modernisation Act. It has been said in hindsight that thanks to the pressure of Citigroup, this Act was passed too quickly and no adequate measures were taken to prevent allfinanz firms' conflicts of interest. This might have contributed to the many Wall Street and mutual fund abuses that took place in the late 90s / early 2000s⁸¹.

Citigroup has also lobbied on issues such as market access / free trade areas (China Trade Bill, NAFTA, FTAA), investment protection⁸², U.S. student lending policies⁸³, financial privacy, bankruptcy reform and terrorism reinsurance⁸⁴. Most lobbying occurs through donations and contributions to the U.S. Presidency, the Congress and the Senate, but Citigroup also lobbies at the World Trade Organisation, especially regarding the GATS⁸⁵, at the International Chamber of Commerce and at the European Commission. The Group organises lobbying activities whenever new regulation or legislation is discussed for the U.S. financial industry, and always aims to reduce government intervention to a minimum. Lobby groups have to convince legislators that the industry can regulate itself, and if legislation is unavoidable, they have to make sure it is favourable to Citigroup's interests.

⁸⁰ Source: Citigroup website, <http://www.citigroup.com/citigroup/press/2003/031010c.htm>

⁸¹ Source: Slate, Sandy Weill: How Citibank's CEO rewrote the rules so he could live richly, Nov. 20, 2002, <http://slate.msn.com/id/2074372/>

⁸² Source: Transnationale website, www.transnationale.org, 4 July 2003

⁸³ Source: LENDING A HAND: A Report on the Lobbying Expenditures and Political Contributions of the Five Largest Student Loan Corporations, <http://www.pirg.org/highered/LendingaHand.pdf>, 10 June 2004

⁸⁴ Source: Center for Responsive Politics, www.opensecrets.org

⁸⁵ GATS = General Agreement on Trade in Services

In the U.S., the financial services industry is the largest lobbying sector, spending nearly \$230 million on lobbying during the 1999-2000 election cycle (compared to \$60 million by the defense industry, for example). Over the last 15 years Citigroup has spent nearly \$17 million on lobbying during election cycles, making it the 20th biggest donor to political parties for that period. The Group donates about as much money to the Democrats as to the Republicans⁸⁶.

Citigroup has had a huge influence on financial trade liberalisation and deregulation. The company was key to the creation of the GATS and even of the WTO itself. In 1997, David Hartridge, then director of the services division of the WTO, said: “Without the enormous pressure generated by the American financial services sector, particularly companies like American Express and CitiCorp, there would have been no services agreement and therefore perhaps no Uruguay Round [the negotiations that led to the WTO's creation] and no WTO”⁸⁷.

Opponents of the deregulation of the financial sector fear that powerful financial firms like Citigroup will monopolise global financial markets, decrease consumer and social protections, and increase economic instability. While the GATS agreement is still relatively weak, Citigroup is trying its best to push for further liberalisation of trade in services through various ways: the company is a member of the influential U.S. Coalition of Service Industries, has a seat in the U.S. Department of Commerce Industry Sector Advisory Committee (ISAC), and sponsored the 1999 World Services Congress and Services 2000, a business - government dialogue that took place in 2002⁸⁸.

According to the Multinational Monitor, there are many examples that suggest that lobbying by Citigroup is shifting the balance of power away from governments and towards the Group, sometimes leading to inadequate protection of consumers and societies around the world. Companies are in the first place designed to make a profit, and sound regulation is needed to ensure this goal is achieved in an ethical manner. Too much lobbying might therefore lead to results that are undesirable from society's point of view. For instance, in the case of bankruptcy reform, Citigroup is pushing Congress to adopt a bill that guarantees repayment of consumer debts to banks, even if this means the consumer in question is unable to pay his other obligations, like housing costs and child support. Such legislation will put consumers at a large disadvantage compared to their creditors⁸⁹.

⁸⁶ Source: Center for Responsive Politics, www.opensecrets.org

⁸⁷ Source: Multinational Monitor, Citigroup: Bankrupting Democracy, April 2002, Volume 23, Number 4, <http://multinationalmonitor.org/mm2002/02april/april02corp3.html>, 10 June 2004

⁸⁸ Source: Multinational Monitor, Citigroup: Bankrupting Democracy, April 2002, Volume 23, Number 4, <http://multinationalmonitor.org/mm2002/02april/april02corp3.html>, 10 June 2004

⁸⁹ Source: Multinational Monitor, The Private Government of Citigroup, April 2002, Volume 23, Number 4, <http://multinationalmonitor.org/mm2002/02april/april02editorial.html>

Executive compensation

For years in a row, criticism has been raised about Citigroup's executive compensation policies by shareholders and other interested groups. Especially Responsible Wealth, a shareholder network, has repeatedly voiced concerns about excessive benefits for Citigroup's top management. In 2004, the group filed a shareowner resolution at the annual meeting, asking Citigroup to tie senior management pay to social responsibility performance as well as to financial performance⁹⁰.

In 2003, Citigroup's former CEO Sandy Weill made \$30 million in cash, which was probably the largest cash payout to a corporate executive in history. That year he also received \$14 million in bonuses and stock options⁹¹. While it is true that Citigroup made record earnings that year, and compensation is usually tied to performance, the height of Citigroup executive pay has caused public indignation.

1.3.2: Corporate citizenship issues

Apart from the many corporate governance issues that have been mentioned above, Citigroup has also often been accused of causing harm to the environment and to (specific groups in) society. The most important corporate citizenship issues of the last 5 years will be discussed below.

ENVIRONMENTAL ISSUES

As a major investor in fossil fuels, mining and logging activities, Citigroup has helped destroy fragile ecosystems, has accelerated global warming, and has caused the displacement of dozens of local communities. Many environmental groups, Rainforest Action Network in particular, have organised campaigns against Citigroup and have informed the public about the destructive projects that Citigroup has funded over the years. Some of these projects are:

Fossil fuels

Caspian BTC pipeline

⁹⁰ Sources: institutional shareowner, June 25, 2003. CEO pay goes up in 2002 while the stock market goes down. <http://www.ishareowner.com/news/article.cgi?sfArticleId=1156>, 12 September 2003; Social Funds, Citigroup shareowner resolutions yield mixed results, 4 May 2004, <http://www.socialfunds.com/news/article.cgi/article570.html>, 12 September 2003; www.responsiblewealth.org, 23 June 2004

⁹¹ Source: New York Times, For Wall Street Chiefs, Big Paydays Continue, March 23, 2004

The Baku-Tblisi-Ceyhan pipeline runs from the Caspian Sea through Azerbaijan, Georgia and Turkey to the Mediterranean Sea, and will transport one million barrels of oil per day by 2005. The project is very controversial because of the environmental and social risks attached to it. The pipeline runs through several protected ecological areas that harbour many different animal species and are at the same time a source of income to local populations. Possible oil spills would have a devastating effect on both the ecology and the economy of these areas. Opponents also worry that the pipeline may worsen national political problems in the three countries, and that it will not bring the promised economic benefits for the local populations.

Citibank was one of 15 banks in an international consortium that backed the BTC pipeline with a \$1 billion dollar loan in February 2004, just one month after Citigroup had adopted its GCIB Environmental and Social Risk Management Policy. According to many NGO's, the project would not even qualify for a loan under the Equator Principles, let alone under Citigroup's even stricter environmental and social credit lending criteria⁹².

Citigroup has devoted an entire page in its Citizenship Report 2003 to explain why it thinks the BTC project is environmentally and socially acceptable. On page 39, it reads that the BTC pipeline is "the first Category A project to be financed by banks that have adopted the Equator Principles". Reasons for the financing are that "[t]he long-term economic benefits for the region are enormous", and that, according to internal evaluations, "the project was in compliance with the Equator Principles and did follow IFC Safeguard Policies". Citigroup indicates that "people can differ on conclusions" about the acceptability of the project, but that the banks, the international financing agencies and the host governments involved all decided that the project offered sufficient environmental and social protection and should be carried out.

Chad-Cameroon oil pipeline

From 1996 until 2001 Citigroup was a financial advisor to an international consortium developing a pipeline transporting oil from Chad to the coast of Cameroon. The construction of the pipeline has met a lot of resistance from the local populations, the media, and from national and international NGO's. In Cameroon, the pipeline runs through pristine rainforests, and poses the risk of forest destruction and pollution. In Chad, the fear exists that the undemocratic government will use the proceeds of the oil to finance civil war and to keep president Deby in power.

⁹² Sources: CEE Bankwatch Network: <http://www.bankwatch.org/issues/oilclima/mainbaku.html>; Corpwatch: <http://www.corpwatch.org/news/PND.jsp?articleid=9329>; Milieudéfensie / Friends of the Earth: <http://www.milieudéfensie.nl/globalisering/publicaties/EarthAlarm%20Bakoe-Tbilisi-CeyhanEnglishversion.pdf>, <http://www.ifc.org/btc>, <http://www.ebrd.com/enviro/eias/regional/18806.htm>, 23 June 2004; BankTrack report "Principles, Profits or just PR?", http://www.banktrack.org/fileadmin/user_upload/documents/0_BT_own_publications/PPP_report_0406_final.pdf, 4 June 2004

The World Bank, who was responsible for a large share of the project financing, approved of the project only after promises had been made by the Chad government to comply with all applicable World Bank safeguard policies, including those on Environmental Assessments, Natural Habitats, Indigenous Peoples, Cultural Property, Resettlement, and Forests. However, there has been continuing controversy about the project because these promises made have not always been met in reality⁹³.

Citigroup argues that the project has the potential of lifting Chad out of extreme poverty, and is convinced that all necessary safeguard measures are respected, that a constructive stakeholder dialogue is taking place, and that the government of Chad will stick to its promise to devote 80% of revenues to priority sectors such as health, education, rural development, infrastructure, the environment and fresh water supply⁹⁴.

Ecuadorian OCP oil pipeline

In Ecuador, an oil pipeline called Oleoducto de Crudos Pesados (OCP) is being constructed with the help of Citigroup. The project will affect several protected forests and wildlife reserves, and poses a major risk to the environment because of the likelihood of oil spills in the earthquake-prone Andes area. The population is afraid the new project will cause pollution, deforestation and diseases among the traditional people that inhabit the area. In communities near the refinery where the oil will be processed, many people are already suffering from cancer and skin diseases caused by contamination⁹⁵.

Citigroup says it is not responsible for the way the project is carried out, because it does not directly finance the project. However, Citibank has arranged a \$200 million loan for an Argentinean oil company, Perez Companc, which is part of the international consortium that is building the pipeline. Without the help of Citibank, Perez Companc would not have been able to participate in the construction of the oil pipeline⁹⁶. Also, Citigroup has issued a financial and an environmental letter of credit for the Ecuadorian Ministry of Energy and Mining, and, according to Citigroup's own information, "members of the OCP consortium are clients of various Citigroup services"⁹⁷.

⁹³ Sources: <http://www.columbia.edu/itc/sipa/martin/chad-cam/>, <http://www.worldbank.org/afr/ccproj/>, http://www.afrol.com/Countries/Cameroon/backgr_pipeline_project.htm, 23 June 2004

⁹⁴ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

⁹⁵ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

⁹⁶ Source: Multinational Monitor, The cost of living richly, April 2002, Volume 23, Number 4; <http://www.amazonwatch.org/amazon/EC/ocp/>, <http://www.ran.org/news/newsitem.php?id=435>, 23 June 2004

⁹⁷ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

Papua New Guinean Gobe oil pipeline

Citibank arranged a loan in 1995 for Chevron and other multinationals to construct an oil pipeline and processing facilities in Papua New Guinea. The loan was refinanced in 2001. The pipeline runs through pristine rainforest and may cause severe ecological damage in the event of a possible oil spill. Also, the project opened up the rainforests to commercial logging companies by constructing infrastructure in previously untouched forest areas. Deforestation in the area may cause soil erosion, water pollution and damage to coral reefs⁹⁸.

Citigroup says that “the resources industry constitutes around 80% of Papua New Guinea’s export revenues and about 25% of GDP, hence the project was beneficial for the country and the standard of living for Papua New Guinea people”⁹⁹. The Group also says that the project complies with the World Bank guidelines for project finance.

Venezuelan oil pipeline

Rainforest Action Network has protested against Citigroup’s involvement in the construction of an oil pipeline in the Orinoco River Delta by Petrozuata, because of the environmental risks of the project and the harmful consequences for the indigenous people living in the area¹⁰⁰.

Citigroup has responded by clarifying its relationship with Petrozuata, which is a joint venture between the companies Conoco (U.S.) and Petr leos de Venezuela. Citigroup was, according to its own information, a financial advisor to the joint venture until 1997 and acted as an underwriter for its bonds. According to Citigroup, the oil pipeline project complied with all local regulations and with “substantially all World Bank environmental standards”. The project took various measures to reduce its environmental impact, including planting eucalyptus trees around the oil facilities to offset emissions. Petrozuata’s plan was to plant 30,000 acres of eucalyptus trees by 2004, and to harvest 5,000 trees each year to “reduce Venezuela’s dependence on imports for paper pulp and timber”. A Petrozuata affiliate, Agroforestal, is said to contribute to the construction of schools and health care facilities to help the local population¹⁰¹.

Baltic Lukoil D6 oil project

⁹⁸ Source: Multinational Monitor, The cost of living richly, April 2002, Volume 23, Number 4

⁹⁹ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

¹⁰⁰ Source: Rainforest Action Website, www.ran.org, 28 May 2004

¹⁰¹ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

In the Russian enclave Kaliningrad, which borders with the Baltic Sea, the Russian oil company Lukoil has started an oil drilling project in March 2004. In 1983, drilling tests in this area had caused an oil spill into the Baltic Sea that caused great damage to the environment, including to a national park called the Curonian Spit. Now that Lukoil is exploiting the oil reserves, local inhabitants fear that a similar environmental disaster might occur. The people of Kaliningrad only had limited access to information about the project when the Environmental Impact Assessment was carried out and have not been consulted during the assessment.

Even though consultation of local interest groups and transparency are prerequisites for financing by any of the Equator Banks, several of these banks participated in an international loan syndicate providing \$765 million in the form of a long-term debt facility to the project in November 2003. Citigroup was one of two banks that arranged the debt facility¹⁰².

Thai Ratchaburi power plant

Citibank assisted in the privatisation of the Ratchaburi Electricity Generating Company of Thailand in 2002. The power plant processes gas from neighbouring Burma, where the proceeds of natural gas sales are used to back the repressive military regime that is in power. It is also said that the regime has used forced labour for the construction of the gas pipeline and pipeline-related infrastructural projects. Besides that, the pipeline is running through forests of great ecological value, and it is feared that no adequate safety measures are in place to prevent disastrous leakages or explosions¹⁰³.

In 2004, a group of Citigroup shareholders filed a resolution at the annual meeting asking the Group to report on its relationships with companies doing business with Burma. The shareholders suspected that the financing for the Ratchaburi power plant might be in violation of U.S. government sanctions against Burma's military regime¹⁰⁴.

Citigroup has commented that its involvement in Ratchaburi is limited to the power plant, and that it "explicitly refrained from any involvement in the pipeline project"¹⁰⁵.

Indian Dabhol power plant

¹⁰² BankTrack report "Principles, Profits or just PR?", http://www.banktrack.org/fileadmin/user_upload/documents/0_BT_own_publications/PPP_report_0406_final.pdf, 4 June 2004

¹⁰³ Source: Multinational Monitor, The cost of living richly, April 2002, Volume 23, Number 4

¹⁰⁴ Source: Social Funds website, Citigroup shareowner results yield mixed results, May 4, 2004. <http://www.socialfunds.com/news/article.cgi/article570.html>, 12 September 2004

¹⁰⁵ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

Citigroup arranged a finance deal for the Indian Dabhol power plant, which has been widely criticised in India and in the U.S. The U.S. public was interested in the project because Dabhol was majority owned by Enron, and the environmental, social and economic trouble surrounding the power plant even led to inquiries by the Committee of Government Reform of the U.S. House of Representatives in 2002.

Besides many financial problems, a general lack of transparency and allegations of corruption, Dabhol was a controversial project because the power plant caused water pollution, and because the project displaced thousands of people without offering them any compensation. Further human rights violation occurred when peaceful demonstrations by local villagers were met by aggressive security forces which were paid by Dabhol and Enron¹⁰⁶.

Peruvian Camisea gas pipeline

Citigroup was the financial advisor for the financing arrangement of the Camisea gas development project in Peru in 2001/2002. This project was initiated by Shell and Mobil in 1996, but these two companies decided not to go through with the gas pipeline after their own environmental risk assessments had proven that it could have destructive effects on the surrounding pristine forests and their inhabitants. Preliminary research in the area had actually killed many indigenous people because they were exposed to diseases that were previously unknown to them, like small pox and influenza¹⁰⁷.

Shell's Environmental Impact Assessment found that "loss of food resources, contamination of drinking water supplies, diseases, loss or damage to archeological sites and changes to existing economic activity could occur as a result of the project"¹⁰⁸. However, the Peruvian government approved of the project in December 2001 despite protests from indigenous people, while the actual construction of production sites had already commenced earlier in 2001.

In a comment on its involvement with the project, Citigroup stresses the economic benefits the project will bring to the country and says that in its role as a financial advisor, it has promoted stakeholder dialogue and compliance with the projects' environmental management plan¹⁰⁹.

¹⁰⁶ Sources: http://www.house.gov/reform/min/pdfs/pdf_inves/pdf_admin_enron_dabhol_fact_sheet.pdf, http://www.asia.citibank.com/asia/index/hm_index/1,3800,5-en-ps-5,00.html, 23 June 2004

¹⁰⁷ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

¹⁰⁸ Source: Multinational Monitor, The cost of living richly, April 2002, Volume 23, Number 4

¹⁰⁹ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

Logging

Indonesian palm oil plantations

Citigroup is a business partner of the Indonesian palm oil company LonSum, which is responsible for clearing vast areas of tropical rainforest in Indonesia, causing out-of-control forest fires, pollution, and soil erosion. Palm oil plantations in Indonesia are also threatening the habitats of several endangered species, including the orang-utan. The conduct of LonSum has violated national and international norms through illegal logging and human rights abuses. Many indigenous people have been forced to move because of the conversion of their land into plantations¹¹⁰.

Citigroup's involvement with the Indonesian palm oil sector will be discussed further in section 2.5.2.

Indonesian paper and pulp industry

Citigroup has invested in Indonesia's largest paper and pulp conglomerate Asia Pulp and Paper (APP). APP has been accused on various occasions for unsustainable logging practices. The company has contributed to the deforestation of large areas of tropical rainforest in Indonesia, threatening the survival of its fragile ecosystems¹¹¹.

Chilean Santa Fe pulp mill

Citigroup's involvement in the forestry sector includes the 1998 acquisition of Chile's Santa Fe pulp mill and forestry operation. SantaFe turns temperate rainforests into wood chips and then replants the forest with eucalyptus¹¹².

Citigroup has commented on its role in the financing of the Santa Fe pulp mill, saying that it recapitalised the company in 1988 after its bankruptcy, "following all regulatory constraints required by the Chilean Forest Service to protect native forests", and that it "sold its 20% stake in 1997 to CMPC, a Chilean paper and pulp producer"¹¹³.

Californian redwoods

California's Headwaters Forests are threatened by Pacific Lumber, a commercial logging company that is clear cutting forests in an unsustainable manner. Salomon Smith Barney

¹¹⁰ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

¹¹¹ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

¹¹² Source: http://www.ecn.cz/zemepredevsim/archive/campaigns/rainforest/rainforest_news-8-01.html

¹¹³ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

has been an important financial advisor to Pacific Lumber, and has even invented a new debt instrument for the company, called 'timber notes'. The activities of Pacific Lumber are threatening several endangered species in the area, and are causing soil erosion and river pollution¹¹⁴.

Mining

Brazilian Amazon mining (CVRD)

Citigroup has been accused of contributing to environmental degradation in the Brazilian Amazon through its involvement in mining activities by the company Cia Vale do Rio Doce (CVRD) in Brazil¹¹⁵.

To this, Citigroup has commented that it has helped with the privatisation of CVRD in 1997 and has held a <2% share in the company since. CVRD used to own several paper and pulp companies but has sold all of these except for one, Celmar S.A., which is now only going to be used for mining and metal production activities.

According to Citigroup, CVRD complies with many high international standards (ISO 14001, British Standard 7750), and "was preparing Environmental Impact Studies and using control procedures even before these were required by law"¹¹⁶. The company also spends \$1.5 million a year on healthcare, education and infrastructure projects for indigenous communities. For all these reasons, Citigroup thinks its involvement in CVRD is in line with its own ethical standards.

Other

Biotech firms

In the fall of 2000, a Seattle based campaign against Citigroup, called Citiaction, was launched to educate people about the controversial CSR issues the Group was involved in. One of many issues raised by Citiaction was Citigroup's involvement in biotech and agribusiness firms like Monsanto, Deltagen, and Orchid Biosciences. These and other biotech firms all got loans from Citigroup¹¹⁷. Their activities are, however, very controversial, and are seen to threaten small farmers and the environment. Genetic modification of crops is rejected by many people who are not convinced of its benefits, and the ethical discussion about this relatively new practice has not led to any convincing conclusions yet.

¹¹⁴ Source: Multinational Monitor, The cost of living richly, April 2002, Volume 23, Number 4

¹¹⁵ Source: website Rainforest Action Network, www.ran.org, 28 May 2004

¹¹⁶ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

¹¹⁷ Source: <http://students.washington.edu/ruckus/vol-4/issue-1/12citiaction.html>, 10 June 2004

Lobbying: environmental regulation

Citigroup has used its influence over the WTO/GATS negotiations to prevent binding international environmental regulations¹¹⁸. The scope and mechanisms of Citigroup's lobbying influence have already been discussed in section 1.3.1 above.

SOCIAL ISSUES

Sale of World Bank bonds

The World Bank has encountered many protests over the last few years from NGO's and civil society groups worldwide, who disagree with World Bank projects and policies in developing countries. The World Bank is pushing for market liberalisation in many countries where governments are unable and / or discouraged by international financial institutions to offset the negative side-effects of such liberalisation. The privatisation of state-owned enterprises, the weakening of labour laws, and a tight control on government spending that threatens the quality of healthcare and education services are all part of the World Bank's economic development package¹¹⁹.

The World Bank gets 80% of the funds for its projects from selling bonds, which are issued by private financial firms like Citigroup's Salomon Smith Barney unit. RAN, Corpwatch, the World Bank Bonds Boycott campaign and other U.S. NGO's all protested against SSB's role in selling World Bank bonds in 2000 and 2001¹²⁰.

Predatory lending

One of the biggest scandals surrounding Citigroup in the U.S. had to do with the predatory lending practices of Associates First Capital, a company which was acquired by Citigroup in 2000. The Associates' consumer finance activities were incorporated into CitiFinancial, making Citigroup the largest subprime lender in the U.S.¹²¹. Subprime lending means that loans are made available at relatively high interest rates to people who usually have difficulty in obtaining loans because they are considered high-risk lenders, like the urban poor, which are mostly elderly people and people of colour. Subprime lending turns into predatory lending if the costs of lending are unnecessarily high and / or if they are not

¹¹⁸ Source: Transnationale website, <http://www.transnationale.org/anglais/fiches/127.htm>, 7 April 2003

¹¹⁹ Source: World Bank Bonds Boycott, http://www.jwj.org/global/S26/Organizing_Kit/jwj_wbbb.htm

¹²⁰ Source: World Bank Bonds Boycott, <http://econjustice.net/wbbb/links/dakarenglish.htm>

¹²¹ Source: Multinational Monitor, Predatory Associates; Citigroup, Predatory Lending and the Credit Crunch for the Poor and Working Class, April 2002, Volume 23, Number 4

transparent to the borrower, who may get into big financial trouble when its time for repaying the loan.

Predatory lending is regarded as a very unethical practice, especially since it affects the most vulnerable groups in society most. After allegations of predatory lending, Citigroup agreed to pay \$240 million to settle accusations that CitFinancial used deceptive practices to sell home loan insurance to customers with a history of unpaid debts in September 2002, and another \$70 million to settle an investigation by the Federal Reserve into its lending practices in May 2004. In the latter case, CitiFinancial was accused of violating fair lending laws by raising the cost of loans to poor customers through refinancing schemes and by requiring them to have unnecessary co-signers¹²².

Over the last few years, Citigroup has taken various measures to prevent future predatory lending practices by its employees, as described in section 1.2.1.1. In May 2004, CitiFinancial's CEO Harry Goff said: "I [...] believe that CitiFinancial today has the best consumer protection programs and policies in the entire consumer finance industry"¹²³.

Apartheid

In the fall of 2002, a coalition of South African civil society groups filed a lawsuit in the New York District Court to 20 American multinationals that allegedly supported the apartheid regime before it fell in 1994. Citicorp was accused of having provided loans to the racist government to fund its police force and its armed forces, which were responsible for countless human rights violations in the country¹²⁴. The people of South Africa now have to pay back these loans through their taxes.

Banamex

In 2001, Citigroup merged its Mexican branch with Banamex, making Citigroup the largest financial institution in Mexico. Besides Banamex' alleged involvement in extensive money-laundering practices, which has been discussed in section 1.3.1, the merger was controversial in several other ways. One criticism has been that the deal provided shareholders with a profit of \$7.5 billion dollars, while Mexican tax-payers were still paying off the banks \$3.8 billion in bad debt. Also, the governor of Mexico City, Andres Manuel Lopez Obrador, accused Citigroup of avoiding taxes on the merger deal¹²⁵.

¹²² Source: Consumer Affairs website article released 28 May 2004, http://www.consumeraffairs.com/news04/citi_fine.tml

¹²³ Source: Consumer Affairs website article released 28 May 2004, http://www.consumeraffairs.com/news04/citi_fine.tml

¹²⁴ Source: Corpwatch website, <http://www.corpwatch.org/article.php?id=4856>

¹²⁵ Sources: Rainforest Action Network website, Citigroup becomes Mexico's largest bank after Banamex merger, 10 August 2001, www.ran.org, 28 May 2004; Associated Press, Mexico: banks bombed to protest taxpayer bailout, 14 August 2001, www.corpwatch.org, 10 June 2004

Prison labour

According to the CitiAction campaign, Citigroup's business unit SSB was the lead underwriter of the IPO of Wackenhut Corrections Corporation, a company which is notorious for contracting out prison labour to the private sector¹²⁶.

Corpwatch, a U.S. non-profit organisation whose goal is to 'hold corporations accountable'

Employee relations

Over the last few years, several incidents have occurred regarding employee relations within Citigroup. One criticism is the frequency of mergers, acquisitions, and reorganisations, which causes thousands of people each year to lose their jobs. 10,000 job cuts a year is not an exception¹²⁷. Although Citigroup's total workforce may remain constant or even increase, the many restructurings still negatively affect the lives of those those who are made redundant in the process.

In 2000, SOMO received an e-mail from a former workers' council member for the staff of a German Citibank call-center, who explained the trouble employees went through after the 1998 merger between Citicorp and Travellers. He said restructurings had led to massive layoffs especially in call-centers in the U.K., Germany and Spain, and that former employees had started a campaign called Citi-Critic. Besides challenging Citigroup's employee policy on an international level, the Citi-Critic campaign wanted to expose Citigroup as a major political power. According to employees, Citigroup was a large sponsor of political parties and the biggest funder of the IMF and the World Bank. In the words of the employee; "Our campaign does not only aim at Citibank as a great union buster, but also at the influence of Citibank on global political decisions, often under the label of 'Washington Consensus'"¹²⁸.

Another employee issue that has haunted Citigroup over the last few years is the large-scale lawsuit against the Salomon Smith Barney unit about sexual harassment. Many women in this business unit have said they feel discriminated and harassed by their male colleagues and managers. The issue was brought to public attention in 1996 when three women filed a class action suit against SSB that became a nation-wide scandal. Especially notorious was the New York SSB 'boom boom room', which was created by the branch

¹²⁶ Source: <http://students.washington.edu/ruckus/vol-4/issue-1/12citiAction.html>, 10 June 2004

¹²⁷ Source: Transnationale website, <http://www.transnationale.org/anglais/fiches/127.htm>, 7 April 2003

¹²⁸ Source: E-mail from ex-Citibank employee to SOMO researcher Myriam Vander Stichele, 4 October 2000.

manager. In this room, sexist comments were frequently made, and women workers were harassed¹²⁹.

Since the 1996 scandals, nearly 2,000 female SSB employees have pressed charges against the brokerage firm. In late 2002, for the first time a female stockbroker was financially compensated when she won her lawsuit and got \$3.2 million from SSB. The panel of arbitrators which is handling the settlement with the 2,000 employees criticized SSB for creating "a work place permeated with discriminatory intimidation, ridicule and insults"¹³⁰. In April 2004, the New York based National Organization for Women (NOW) wrote that "the Smith Barney unit of Citigroup, [is] in the latter stages of a protracted process to resolve mass claims of sex discrimination that were filed in the late 1990s"¹³¹. As far as we know, no final settlement has been made yet¹³².

1.4: General analysis and assessment of Citigroup's CSR policy and practice

A serious fallacy of Citigroup's CSR policy is that the internal mechanisms of implementation are not described in any of the CSR related documents. Only the Code of Conduct touches upon the issue of implementation, but no clear oversight is given of the lines of responsibility within the company and the levels at which CSR policy is created and implemented. The people responsible for implementation cannot easily be traced. Citigroup has a very complicated organisational structure and this causes a general lack of understanding on how the company works for readers who orientate themselves on Citigroup's written publications. For this research, SOMO has not contacted Citigroup directly, so we cannot comment on the dynamics of the flow of information within the company (how quickly do questions reach the right person, how fast can replies be given).

As to the contents of the Group's CSR policy, it is indeed the case that Citigroup's policies have changed a lot over the last few years, a question that was posed at the end of section 1.1.4. In that section, it was noted that Citigroup's CSR ratings ranged from very negative in 2000 and 2001, to very positive in 2003 and 2004. Although our list of rankings may not be inclusive, it does seem indicative of a turn-around in Citigroup's CSR policy. Citigroup did not make it to the Multinational Monitor's list of the World's Worst Corporations in 2003¹³³, nor to any other negative CSR list as far as we know.

Whether Citigroup deserved to be included in so many important positive CSR rankings in 2003 and 2004, remains subject of discussion. The Rainforest Action Network does seem to be very pleased with Citigroup's progress in the area of the environment and related social

¹²⁹ Sources: Multinational Monitor, Breaking the Brokers' Sexual Harassment Culture, April 2002, Volume 23, number 4.

¹³⁰ Source: http://www.iltla.com/2003_VESTED/jan_2003_torts.htm, 9 July 2004

¹³¹ Source: http://www.nownys.com/w&w_news.html, 9 July 2004

¹³² Time of writing: 9 July 2004

¹³³ Source: <http://multinationalmonitor.org/mm2003/03december/dec03corp1.html>,

issues. They have called Citigroup the new industry leader on many occasions¹³⁴. And it is indeed true that Citigroup's policy is among the best-in-class. What will become of this policy in practice, however, still remains to be seen. Many NGOs are closely watching Citigroup's actions to see if the financial giant is really living up to its standards. For instance, the Dutch-based NGO network BankTrack published a report in June 2004, just one year after the first group of banks signed the Equator Principles, to evaluate the implementation of the Principles. In their report, they write that Citigroup's environmental policy has been beaten in May 2004 by Bank of America, which has come up with even stricter standards.

The BankTrack report is generally positive about Citigroup's commitments, and praises Citigroup's internal environmental policy, its promise to reduce carbon dioxide emissions, and the fact that Citigroup is one of only two Equator banks that has hired additional environmental and social staff to see to the implementation of the Principles. According to BankTrack, Citigroup has also introduced the necessary changes in its credit policy to integrate the Equator Principles, and has made compliance with the Principles part of the regular internal audits. On the negative side, BankTrack reports that Citigroup is still involved in several controversial projects, such as the BTC pipeline, the Lukoil D6 project, and possibly an East Siberian gas pipeline¹³⁵. Many NGOs think that these projects do not qualify for financing under the Equator Principles.

In general, it can be said that most environmental and social CSR evaluations only focus on policy, and not on practice. The Dow Jones Sustainability indices, the FTSE 4 Good index, and ethical sustainability funds do not conduct research on the implementation of CSR standards, but only assess the policy itself. This is one reason why NGOs and industry analysts may differ widely on their CSR evaluations of companies. Another reason why Citigroup maybe should not be included in sustainability indices, is that the company remains a very important financier of fossil fuels, mining and other extractive activities, which are unsustainable practices even if measures are taken to reduce greenhouse gases.

As to corporate governance, which has been included as an important part of CSR policy in this SOMO report, Citigroup has also made a lot of necessary adjustments to its policy since 2000/2001. These efforts, according to us, should be seen as an attempt to catch up on common sense ethical standards rather than excellent CSR behaviour. But at least the extreme abuses of the late 90's and early 2000's are finally being addressed, in a way that can generally be judged positively. Citigroup does seem to be willing to cooperate with financial authorities, and although the Group does not plead guilty for its past actions, it takes on responsibility to avoid corruption, fraud and conflict of interest and predatory lending activities in the future.

¹³⁴ Source: www.ran.org

¹³⁵ BankTrack report "Principles, Profits or just PR?", http://www.banktrack.org/fileadmin/user_upload/documents/0_BT_own_publications/PPP_report_0406_final.pdf, 4 June 2004

A final note on Citigroup's CSR policy is a critical one: all adjustments that Citigroup makes are first and foremost in its own self-interest. Strict corporate governance policy serves the goal of repairing Citigroup's severely damaged image and regaining the confidence of consumers, as well as avoiding binding industry regulations. Pro-active corporate citizenship initiatives like a strong focus on financial education of disadvantaged groups, a strong focus on Hispanics, and the efforts to promote micro-finance and cheap housing projects are all part of the long-term strategy of Citigroup. Each of the targeted groups represents an interesting business opportunity in the long run.

It is not necessarily a bad thing that Citigroup binds its own future to the future of these disadvantaged groups; their success will ultimately influence the Group's success. In contrast with many other banks, Citigroup's strength lies in its large consumer base. The Global Consumer Group provides 55% of Citigroup's income. This is a large portion in an industry where most companies only rely on a relatively small portion of society to provide most of the corporate income. The large consumer base has the additional advantage that it provides more financial stability to the company than reliance on other client groups would. During economic downturns, income from investment banking and management may drop sharply, but income from consumers will remain stable. People will always need bank accounts, mortgages and credit cards...

PART 2: Citigroup in Indonesia

2.1: Methodology

For this section, different sources of information were used, including Citigroup's own website and press releases from the Indonesian media. However, one source was of special significance: Business Watch Indonesia's (BWI) research on Citigroup in Indonesia, as put down in their reports 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations: A Case Study of Indonesia', and 'Another side of Citibank', which were written in 2003 and revised in 2004. BWI is an Indonesian NGO that was set up in 2002 to promote democratic economic governance. The research on Citigroup was conducted by BWI's own personnel, with the help of four experienced Indonesian journalists. The reports are based on desk research and on various telephone, e-mail and face-to-face interviews with Indonesian business analysts, social analysts, LonSum management and Citibank management and employees, which were conducted in the fall of 2003. More information on Citigroup's involvement in the Indonesian oil palm industry can also be found on the website of Rainforest Action Network, www.ran.org.

2.2: Citigroup in Indonesia; an introduction

In Indonesia, the financial sector is dominated by the banking sub-sector. Other financial services, like insurance and pension fund management, only comprise a small part of the financial market. To get an idea of the relative size of these activities: in 2002, banking covered 90 % of the private financial market, insurance 3% and pensions also only 3%¹³⁶.

Within the banking sector, state banks and private banks have traditionally fulfilled different roles. Basically, private banks have focused their attention mainly on large corporate clients, and state banks have served more small enterprises and individual clients. For instance, in March 2003, state banks accounted for some 75% of all credits provided to small and medium enterprises (SMEs), while private banks only provided 25% of these credits¹³⁷. Of the private banks, *foreign* banks provided only 0.005% of their total credit to SMEs in 2003, and were usually based in Jakarta only. This reaffirms that their main interest is not with small clients, but rather with large, high net-worth clients.

Citigroup seems to be an exception to this rule: it has quite a large consumer base in Indonesia. The company has been present in Indonesia since 1968, and currently operates three divisions in the country: Citibank, Citigroup Global Markets (formerly Salomon Smith Barney) and Citigroup Private Bank. These divisions offer banking, investment and insurance services to 1.3 million individual customers and 1,200 businesses in the

¹³⁶ Source: Business Watch Indonesia, based on InfoBank, Nr. 292 - August 2003, Vol.XXV.

¹³⁷ Source: 'Critical issues in the financial industry', SOMO financial sector report, 2004. Chapter 3: *The case of Indonesia*, Myriam vander Stichele.

country¹³⁸. While Global Markets and the Private Bank only have a presence in the capital Jakarta, and focus on wealthy clients, Citibank is one of the 10 largest banks in Indonesia measured by asset size and has twelve branch offices and 45 ATM machines in 5 cities: Jakarta, Surabaya, Bandung, Medan, and Semarang. The bank is doing well financially despite the economic turmoil in Indonesia that started in 1997, and it is generally felt it serves its customers well¹³⁹. In total, Citigroup employs 1,300 employees in Indonesia¹⁴⁰.

According to a senior manager of Citibank, the consumer banking division is currently focusing on attracting as many large individual clients as possible. The savings collected from major customers “are then to be invested in the form of retail credit such as credit cards, home ownership loans and the like”¹⁴¹. This way, Citibank does not have to generate profits from small retail clients by charging them high fees for transactions, but can let the large clients provide the capital needed to invest in retail credit. Since the economic crisis of 1997, Citibank apparently has been more careful with providing credit to local companies, and focused its attention more on the large multinational companies with presence in Indonesia, like Coca Cola, IBM, and ARCO (a U.S. oil company which has recently been bought by Beyond Petroleum)¹⁴².

As to Citibank’s corporate structure outside the U.S., it can be said that the company assigns different areas of work to local, regional and head offices, as shown in the following table¹⁴³:

Values	Strategies	Tactics
Head Office		
	Regional Office	
		Local Office

The head office, according to this table, can only make decisions about the overall values of Citibank, for instance brand image and the standardization of products and services. The regional offices regulate business sector strategies, and decide where the focus of Citigroup’s activities in a specific region should be on. The local offices work out the specific tactics on how to conquer a national market.

¹³⁸ Source: Citigroup website, ‘Countries’, Indonesia, www.citigroup.com, 7 July 2003

¹³⁹ Source: BWI, ‘Another side of Citibank’, January 2004, p. 14

¹⁴⁰ Source: Citigroup website, ‘Countries’, Indonesia, www.citigroup.com, 13 June 2004

¹⁴¹ Source: BWI, ‘The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION’ , January 2004, p. 7

¹⁴² Source: BWI, ‘Another side of Citibank’, January 2004

¹⁴³ Source: BWI, ‘The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION’ , January 2004, p. 5

The lines of responsibility for branches outside the U.S. mainly involve the President Director of each local office, the other Directors, and the Citibank Regional Office. For instance, for Indonesia, there is one President Director and 18 other Directors, each of which has its own superior in the Regional Office, in accordance with his or hers specific field of work. Every decision a Director makes has to be approved of by the President Director and by the relevant Regional Office supervisor. Also, any orders of the President Director to the other Directors have to be approved of by the relevant Regional Office supervisors. So for every decision, all three management levels are involved, and final responsibility lies with the Regional Office¹⁴⁴.

In Indonesia's Citibank, the common practice is that superiors have regular meetings with their subordinates. During these meetings, the performance of the subordinate is evaluated, and the subordinate can indicate if he or she is satisfied with his/her position. Promotions are decided upon according to the capabilities of the employee. If the employee is considered capable for a higher position, but lacks certain necessary job skills, training may be offered. Furthermore, every superior in Citibank Indonesia is assessed by his or her subordinates. The performance of managers is measured through online polls among employees¹⁴⁵.

The highest Citigroup officials that are responsible for Indonesian operations are Stephen Long (Asia Pacific Group Head for the Corporate Bank), Alan Harden (Asia Pacific Group Head of Asset Management), and Frits Seegers (Asia Pacific Group Head for the Consumer Bank)¹⁴⁶. Frits Seegers, originally from the Netherlands, carries the final responsibility for Citibank Indonesia's performance.

Since 1999, Citibank has had a special community program in Indonesia, called Citibank Peka. It is basically the local branch of the global Citigroup Foundation. Just as the Foundation, Citibank Peka focuses on (financial) education and microfinance initiatives. The activities of Citibank Peka are further described in the next section.

2.3: Citibank Peka

¹⁴⁴ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION' , January 2004, p. 7

¹⁴⁵ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION' , January 2004, p. 6

¹⁴⁶ Source: Citigroup internal information about a 2002 business meeting in Hong Kong, <http://events5.broadcastone.net/citigroup/20020121/sessiondetails.htm>

Citibank Peka activities are based on two pillars: providing funds to local NGO's and contributing to projects through the work of Citibank volunteers. In 2001, Citibank Peka was involved in the following projects¹⁴⁷:

	Project	Foundation	Value (US\$)
1.	Citibank Peka Street Kids Program	Bintang Pancasila Foundation	7,600
2.	Citi Teacher's Awards Program	Mitra Mandiri Foundation	35,000
3.	Electronic Dictionary (for blind persons)	Mitra Netra Foundation	18,000
4.	Citibank Peka Street Kids Program	Nanda Fian Nusantara Foundation.	7,600
5.	Citibank Peka Street Kids Program	Usaha Mulia Foundation	7,600
6.	Microcredit Program	Grameen Foundation	75,000
7.	School Rebuilding Program, Bengkulu	Mitra Mandiri Foundation	10,000
8.	Capacity Building Program	Mitra Mandiri Foundation	20,600
9.	Peka Volunteer Program	Mitra Mandiri Foundation	10,500
		Total	191,900

The funds that are made available to these NGO's come from the Citibank Foundation. The contribution to the Grameen Foundation that is listed in the table above is part of a \$1 million dollar grant that was given to the Foundation in 1999, in order to develop micro businesses in Indonesia, Malaysia, the Philippines, South Korea and Thailand. The grant is used for providing training to NGO's who are interested in applying the Grameen microfinance method¹⁴⁸.

The capacity building program focuses on training to local NGO's, in the areas of financial management, network building and fundraising, and volunteer mechanisms. The street kids program concentrates on educating elementary school students. The electronic dictionary is meant as a tool for the education of young and old blind Indonesians.

Some other examples of Citibank Peka projects are the partnership with the University of Indonesia, where Citibank employees give lectures, and the special classes that are given by Citibank Directors to street children.

At the moment, in 2004, Citibank Peka has expanded some of its activities and partnerships, and is now working with 15 local NGO's, largely on the same issues of education and microfinance that it has been involved in since 1999. In 2001 and 2002, Citibank Peka received three awards for its community programs, amongst them the 'Outstanding Global Corporate Leadership Award 2002'¹⁴⁹.

¹⁴⁷ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION' , January 2004, p. 9

¹⁴⁸ Source: Citigroup website, 'Countries', Indonesia, www.citigroup.com, 29 January 2004

¹⁴⁹ Source: Citigroup website, 'Countries', Indonesia, www.citigroup.com, 12 June 2004

According to research by Business Watch Indonesia, the Citibank Peka community program is not very transparent, because of some organisational characteristics. Apparently, each Citibank Indonesia division “develops its own work plans in line with those of the respective division in the regional office. Therefore, each division, such as corporate credit or retail credit, has no idea of how much budget is put aside by the other divisions”¹⁵⁰.

Now that the positive contributions of Citibank to Indonesian society have been described, it is time to look to some negative findings of the BWI report on Citigroup. Before getting into the specific details, it is useful to identify the most common issue areas in the Indonesian financial sector, or in other words, the Corporate Social Responsibility issues that multinational financial firms usually face there.

2.4: Issue areas in the Indonesian financial sector

In developing countries like Indonesia, multinational financial firms face other Corporate Social Responsibility issues than at home due to different economic, social, political, environmental and cultural circumstances. Usually, because of weak national legislation and enforcement, CSR programs in the developing world first have to cover basic ethical questions, such as how to avoid *corruption* in all levels of business, and whether or not the company is respecting basic *labour rights* such as the right to organize and the right to severance pay. Furthermore, because of the specific character of many developing countries’ economies and economic sectors, CSR issues regarding *privatisation* and *environmental degradation* are often considered CSR priorities. These four issue areas, applied to Indonesia, will be briefly discussed below.

Corruption

Corruption issues in Indonesia are very complicated since the economy is still ruled by powerful families and their friends, who become extremely rich while the rest of the population is basically standing at the sidelines. Almost every multinational operating in Indonesia is confronted with this national dichotomy and is easily accused of taking sides with the wealthy part of society. The same is true for Citigroup, who has managed funds for two of former president Suharto’s three daughters in the past. The Suharto family is notorious for its utterly corrupt behaviour¹⁵¹, and handling their money is easily associated with fraud, unfair competition, and money laundering practices.

¹⁵⁰ BWI, ‘The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION’ , January 2004, p. 10

¹⁵¹ For an interesting overview of the Suharto family’s business dealings, see <http://www.washingtonpost.com/wp-srv/business/longterm/asiaecon/stories/sons012598.htm>

Also, a Citibank insider, in a private conversation with an Indonesian journalist, admitted that during Suharto's New Order era, Citibank was closely related to large Indonesian conglomerates like the Salim Group (controlled by Liem Sioe Liong), the Sinar Mas Group (controlled by Eka Tjipta Widjaya) and the Gadjah Tunggal Group (of Syamsul Nursalim)¹⁵². All these groups' leaders were close friends to Suharto and became extremely rich during his presidency. Since the fall of the Suharto regime in 1998, these conglomerates have increasingly come under public scrutiny for their involvement in widespread corruption among the Indonesian business elite. One of the allegations was that the groups enriched themselves through public money, at the expense of the Indonesian population.

It is a difficult question to what extent financial firms should be held responsible for the behaviour of their clients. However, there are a few things that multinational financial companies should definitely do (or not do) when operating in a country where corruption is widespread. For instance, financial firms should never accept any kind of gift or favour from their clients, whether before or after providing financial services to these clients. Financial firms should also avoid cooperating with or facilitating possible corrupt practices by their clients.

It is reasonable to ask financial firms to be aware of the reputation of their clients, and that they be very careful with helping those clients who are known to be corrupt. Just like environmentally unsound behaviour and human rights violations, corruption is a risk to financial firms. Getting involved with corrupt businessmen can damage a company's reputation and make the local population lose their confidence in its brand name. Corruption is also a big economic risk, since corrupt business practices are per definition characterised by a lack of transparency and accountability. When corruption is brought to the light, clients often find themselves in financial trouble¹⁵³. Thus, company's like Citigroup should not hesitate to withdraw from companies that it thinks are corrupt.

Finally, multinational financial firms should do their very best to make sure all their transactions, investments and involvements are transparent and can be accounted for. This is especially true for countries where corruption is a sensitive issue, like in Indonesia, where a lack of information will cause suspicion. Any type of business relation with the corrupt elite or with controversial companies or projects may damage a financial firm's reputation in Indonesia, whether or not the business relationship implies direct responsibility of the financial firm for the actions of its clients.

Most corruption issues are covered by Citigroup's Code of Conduct. However, the last point about transparency is not covered by the Code. Just as many other financial firms, Citigroup often protects the identity of its clients for reasons of confidentiality. This poses a difficult conflict of interest between legal requirements, banks' wishes to maintain a

¹⁵² Source: BWI, 'Another side of Citibank', January 2004

¹⁵³ For instance: the value of the shares of their company collapses, huge fines have to be paid, financiers pull out their investments etc.

good relationship with their clients, and the public's desire to know what is going on. Especially in countries like Indonesia, where corruption is high on the political agenda, Citigroup could consider making a policy of disclosing client relations to the public when legally possible.

In Indonesia, according to BWI, the old Banking Confidentiality Law which granted banks the right to keep the names of their clients to themselves was revised in 2002. The public is now entitled to know the names of a bank's debtors and customers, but not the amount of the loan or the deposit. However, during its own research, BWI encountered resistance from Citibank personnel, who refused to disclose their debtor's and customers' names¹⁵⁴.

Labour rights

Labour rights in the Indonesian financial services sector are generally okay, but if national legislation in this area is not enforced properly and companies do not have very clear standards on this topic but are just following national regulations, the position of employees can still be weak. In effect, it means that the implementation of labour rights is left over largely to local management.

Although the reporting and evaluation mechanisms as described in section 2.1 above are considered good corporate practice, Citibank employees have also encountered some problems with their management in recent years. Interviews conducted by BWI with employers and employees at the end of 2003 revealed that working conditions were judged positively on most aspects, like corporate structure and career development, but that the negative attitude of managers towards the idea of a workers' union was considered a great problem by some.

There are, of course, no written rules that prohibit the forming of a workers' union at Citibank, but employees argue that management does not approve of union initiatives. It is felt that employees' efforts to organise themselves meet resistance at different levels of management¹⁵⁵. Citigroup should therefore carefully see into issues of labour rights, including the right to form a union, especially in countries like Indonesia, where weak national legislation and enforcement and local cultural attitudes on this issue increase the chance of non-compliance with international regulations on the matter.

Privatisation

As to privatisation, this has been the cause of social unrest and major popular concern in many developing countries, including Indonesia. Commonly heard complaints are that multinationals are taking over economic and political control, are exploiting the population and are so powerful that they are always the winning party in negotiations, business

¹⁵⁴ Source: BWI, 'Another side of Citibank', January 2004, p.1

¹⁵⁵ Source: BWI, 'Another side of Citibank', January 2004, p. 13

transactions and conflicts with governments and government agencies. Over the past few years, enough evidence has been gathered on this topic to understand why local populations are at least afraid of, if not opposed to, multinationals operating in their country.

For Indonesia, privatisation efforts really took off when Suharto, in his last year of presidency (1998), signed several documents committing Indonesia to IMF policies for economic reform. Economic deregulation and the privatisation of state owned enterprises (SOEs) were major promises the government made as part of the conditions for an IMF recovery package. On a national level, there was no stakeholder dialogue, and the government hardly made any efforts to explain the costs and benefits of privatisation to the public.

While privatisation efforts strengthened over the years, public resistance to privatisation also increased. Managers of state owned enterprises, local leaders, and employees of state owned enterprises all tried to stop the privatisation process. Their main fears were that they would lose their jobs, and that foreigners would take over control over their land, capital and lives. For the Indonesian population, memories of colonialism made the takeover of national companies by foreigners a particularly sensitive topic. Other issues were the complete lack of transparency of the whole reform process and the involvement of the IMF, that was thought to put its own interests (repayment of Indonesia's loans) before the interest of the Indonesian people¹⁵⁶¹⁵⁷.

When privatisation deals were closed, the lack of transparency of the sale, the suspicion of corruption, and the price obtained for the previously state owned enterprise were often issues of hot debate in Indonesia. It was felt that the sales of SOEs did not generate the promised revenue, but that the government only lost money through its privatisation efforts, and that in the end, it was the Indonesian population who bore the costs of economic reform. For instance, in 2002, instead of waiting for a more favourable business climate to make a good deal with investors, the government rushed into the sale of the telecommunications company Indosat to meet its IMF targets for that year¹⁵⁸.

In 1998, the Indonesian government announced a list of eight financial institutions that would serve as advisors for the privatisation process. According to government officials,

¹⁵⁶ Source: Nicola Bullard, Focus on the Global South: 'Indonesia's privatisation plans run into troubled waters', <http://www.focusweb.org/publications/1998/Indonesia%92s%20privatisation%20plans%20run%20into%20troubled%20waters.htm>

Milbank, Tweed, Hadley & McCloy, 'Privatisation in Indonesia in an era of change', http://www.milbank.com/news/pdfs/030801_Indonesia.pdf, 14 June 2004

¹⁵⁷ Source: Nicola Bullard, Focus on the Global South: 'Indonesia's privatisation plans run into troubled waters', <http://www.focusweb.org/publications/1998/Indonesia%92s%20privatisation%20plans%20run%20into%20troubled%20waters.htm>

¹⁵⁸ Milbank, Tweed, Hadley & McCloy, 'Privatisation in Indonesia in an era of change', http://www.milbank.com/news/pdfs/030801_Indonesia.pdf, 14 June 2004

the choice of advisors was done in a professional and transparent manner and based on the firms' previous experience with privatisation efforts. All the advisors were foreign owned multinationals, one of them being Salomon Smith Barney¹⁵⁹.

One of the deals that Salomon Smith Barney was engaged in was the largest merger and acquisition deal in Indonesian history, when in 2001 the country's two biggest telecom companies Indosat and Telkom made a \$1.5 billion swap agreement to end cross-shareholdings in some of their subsidiaries. The deal was made to prepare both companies for their privatisation¹⁶⁰. When Indosat was sold in December 2002, Citibank managed the transaction and charged \$18,939 million for its services. Also, \$25 million of the total of \$627.3 million that the Indonesian government received for its shares is still being kept in a Jakarta Citibank account¹⁶¹.

No other instances of Citigroup's involvement with privatisation in Indonesia were found. However, as one of eight financial advisors to the Indonesian government, it is suspected that the Group was in on many of the privatisation deals that have been reached in the past few years, whether as an advisor through Salomon Smith Barney (now Citigroup Global Markets) or through Citibank.

As a party to these deals, Citigroup carries co-responsibility to make sure the privatisation processes it advises on are conducted in an open and transparent manner, and that the outcome of negotiations is fair, and takes into consideration the interest of all affected stakeholders, including the Indonesian population. To date, Citigroup has not issued any statement on its responsibility in privatisation efforts. For countries like Indonesia, a similar statement would be a useful starting point for an open discussion about the costs and benefits of privatisation.

Environmental degradation

Finally, environmental issues are extremely important for countries that rely on the export of natural resources, like most developing countries do. The extraction of natural resources and the agricultural and forestry industries have resulted in the depletion of resources, the loss of biodiversity, health risk for the local population, economic loss for the local population, and many other problems. A bank that is involved in financing such industries should not be surprised when it meets public resistance from the local and

¹⁵⁹ Source: Nicola Bullard, Focus on the Global South: 'Indonesia's privatisation plans run into troubled waters', <http://www.focusweb.org/publications/1998/Indonesia%92s%20privatisation%20plans%20run%20into%20troubled%20waters.htm>

¹⁶⁰ Source: CFO Asia, Corporate finance, December 2001 spotlight, Deals of the Year, 'Indosat and Telkom's resolution of US\$1.5 billion of cross-shareholdings', <http://www.cfoasia.com/archives/200112-03.htm>

¹⁶¹ Source: BWI, 'Another side of Citibank', January 2004, p. 12

international society. In fact, any link with unsustainable economic activities is a significant reputation risk for the financial firm involved.

In Indonesia, two agricultural sectors in particular are notorious for their destructive environmental impact: the paper and pulp industry and the oil palm industry. Both industries have caused a lot of damage to Indonesia's pristine rainforests, and consequently to delicate ecosystems, biodiversity, and local populations living traditional lives in forest areas. The funding of paper and pulp and oil palm businesses by foreign banks is in many cases contrary to the Equator Principles and to other commitments to sustainability. Nonetheless, Citigroup has been involved with the Indonesian oil palm industry for many years. To see what the problems were, and how they have been handled, is the topic of the next section.

2.5: The case of LonSum

2.5.1: Palm oil industry-related problems

According to BWI's report, there are three main problems related to oil palm plantations in Indonesia. One is forest destruction itself, two is damage to the habitat of (endangered) species, and three is the effect on the lives of the local population.

1. Forest destruction

Over the last 15 years, Indonesia has lost 42 million hectares of tropical forests. A large portion of this area has been cleared to make way for oil palm plantations. In 2002, Indonesia had 30 million hectares of land devoted to oil palm plantations, mostly on the island of Sumatra. This is equal to one third of the total forest area in Indonesia. Only 180,600 hectares of these plantations were owned by local communities, the rest was the private property of large multinational palm oil companies. The production costs of Indonesian palm oil are among the cheapest in the world, which explains why only after Malaysia, Indonesia is the biggest producer of palm oil¹⁶².

The Indonesian government has a bad reputation regarding the conservation of forests. Over the years, officials have put short-term economic interest before long-term sustainability. The government gave away permits to clear millions of hectares of forest area, and even when permits were not granted, and land clearing practices were illegal, little intervention occurred. Large scale corruption among the ruling elite was one of the factors that influenced government policy on oil palm companies¹⁶³.

¹⁶² Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

¹⁶³ Source: World Resources Institute, research report 'The state of the forest: Indonesia', 2002. http://pubs.wri.org/pubs_description.cfm?PubID=3147, 16 June 2004

In recent years, the environmental damage caused by illegal land clearing and the expansion of oil palm plantations has been so obvious that even the government had to admit its effects. Especially from 1997 onwards, forest fires have burnt away vast areas of tropical rainforest in Indonesia, and caused health problems and dislocation among the population. Forest burning, for palm oil companies, is the cheapest way to clear land for their plantations. Even though the government warned to stop forest burning, in March 2000 satellite pictures showed 1,200 fire areas in Sumatra. Palm oil companies like LonSum were accused of having lit many of these.

Although forest destruction in Indonesia sharply declined after the monetary crisis that hit the country in 1997, since 1999 the rate of destruction has slowly been climbing again, reaching approximately 120,000 hectares in 2002 (compared to 225,000 hectares in the peak year of 1996). The decrease was due to a drop in investor confidence after the crisis, because of the economic, political and social instability in Indonesia during 1998-1999, and due to the cancellation of many contracts made during the Suharto era.

Even though the rate of destruction has (temporarily) decreased, the forest destruction that still occurs continues to have substantial negative effects on Indonesia's ecosystems. Areas that are converted into plantation quickly become an environmental hazard. For instance, in West Kalimantan, one million acres of land converted into oil palm plantations use 145,000 litres of insecticide and 5,900 tons of chemicals each year. Some important side-effects of this intensive use of chemical substances are soil erosion and river pollution¹⁶⁴.

2. Damage to the habitat of (endangered) species

The rainforests of Indonesia are a home to many different tropical animal and plant species. To get an idea of the biological diversity of Indonesia: there are only 25 ecological hotspots in the world, which together "contain 44 percent of all plant species and 35 percent of all terrestrial vertebrate species in only 1.4 percent of the planet's land area"¹⁶⁵. One of the hotspot areas is Sundaland, and Indonesia covers 75% of this area. Sundaland contains 82 threatened species and 13 critically endangered species¹⁶⁶. One of these species is the orang-utan. Over the last 15 years, the orang-utan population has decreased anywhere between 30 and 50%, mainly because their habitat disappeared through forest clearing activities.

¹⁶⁴ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

¹⁶⁵ Source: Conservation International website, http://www.biodiversityhotspots.org/xp/Hotspots/hotspotsScience/what_are_hotspots.xml, 14 June 2004

¹⁶⁶ Source: Conservation International website, <http://www.biodiversityhotspots.org/xp/Hotspots/sundaland/>, 14 June 2004

3. The effect on the lives of the local population

In Indonesia, the lives of 65 million people depend directly on the country's forests. Increasingly, their livelihoods are threatened by the expansion of oil palm plantations onto their native lands. More often than not, the forest land on which they depend is cleared by palm oil companies without any previous consultation. Many people are forced to move and to change their sources of income. It is of little use to rebel against the large palm oil companies, because these are often backed by the government, the military and/or the police. It has been proven various times in the past that oil palm companies directly hired local policemen to oppress any resistance from the local population. On several occasions, native people who protested against their land being cleared ended up in jail¹⁶⁷.

2.5.2: LonSum and Citibank

PT. London Sumatera Indonesia Plantation, or LonSum, is an Indonesian agricultural giant producing coconut palm oil, coffee, cocoa, tea, and rubber. Palm oil is the company's most important product, comprising 60% of all produce. LonSum is listed on the Jakarta Stock Exchange under the acronym LSIP. Almost half of the shares are owned by PT. Pan London Sumatera Plantation, a holding company controlled by the Napan Group of the Pribadi family on the one hand and Ibrahim Risjad, a powerful Indonesian businessman, on the other¹⁶⁸. Of LonSum's production, 75 percent is exported. In 2002, LonSum owned a total of 121,000 hectares of oil palm plantations.

After the economic crisis that hit Indonesia in 1997, LonSum got into big financial trouble. The government imposed a 60% export tax, and therefore LonSum was forced to sell a larger part of its produce on the domestic market. Now the company was earning less dollars and more rupiahs, just at a time when the rupiah was devaluating quickly. An additional problem was that LonSum was selling its palm oil by means of forward contracts, in which the price of the oil was agreed upon beforehand. The price LonSum charged in 1998 was below the world market price of palm oil that year. But the government calculated the export tax on the basis of the - higher - market price. So the company's income was declining while taxes were rising. Moreover, LonSum's pre-crisis loans that were still outstanding had to be repaid in expensive dollars. As a result, LonSum defaulted on many of them and only got into deeper financial trouble.

¹⁶⁷ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

¹⁶⁸ Although it was rumored in early 2004 that Malaysian businessman Robert Kuok had bought all of Pan London Sumatera shares. Source: The star online, January 6 2004, 'Kuok buys 47% of Lonsum of Indonesia', 14 June 2004

In 2002 the company started to make a profit again, thanks to rising palm oil prices, but LonSum's huge debt was still outstanding, reaching \$260 million in early 2004¹⁶⁹. However, a debt restructuring process, initially under the auspices of the Jakarta Initiative Task Force (set up in November 1998 by the Government of Indonesia in cooperation with the World Bank, IMF and USAID, to help restructure companies' debts¹⁷⁰) is now underway. In February 2004, LonSum's creditors supposedly approved of a debt restructuring deal, in which 25% of the debt would be restructured through a debt-to-equity swap, 10% through a debt haircut, and the rest through rescheduling until 2007¹⁷¹. However, it has proven very hard to find the exact details on this arrangement, and on the creditors that were involved.

According to an inside LonSum source interviewed by BWI, Citibank is involved in the company's debt swap agreement by acting as the company's 'cashier'. This means Citibank pays LonSum's financial obligations to third parties, and afterwards gets repaid by LonSum¹⁷². But what's more, at the time of the interview in late 2003, LonSum owed Citibank a total of \$99 million dollars in payments on previous loans, which were made directly with Citibank years ago.

Citibank's involvement with LonSum actually goes back to 1994, when Citibank arranged a bridge facility of \$183.5 for Pan London Sumatera Plantation to finance the acquisition of LonSum. This bridge facility was replaced by a syndicate loan in November that year, which was also arranged by Citibank. There were 22 banks in the syndicate. The total loan was refinanced in 1996. That same year, LonSum entered into a swap extension contract with Citicorp Financial Services. Because of the financial trouble of LonSum, the contract was terminated in 1998 and Citibank claimed \$1.3 million from LonSum. In 1997, LonSum issued promissory notes worth \$10 million to Citibank, and also entered into foreign currency forward contracts with Citicorp Financial Services and two European banks. The forward contracts were terminated in 1998 because LonSum could not fulfil its financial obligations, and the three banks claimed a total of \$91 million from LonSum. Finally, LonSum had also entered into a par forward commodity contract with Citibank, and this contract was terminated in 1998 as well, adding another 0.8 million dollars to LonSum's debt to Citibank¹⁷³.

¹⁶⁹ Source: The star online, January 6 2004, 'Kuok buys 47% of Lonsum of Indonesia', 14 June 2004

¹⁷⁰ Source: Bank Indonesia website, <http://www.bi.go.id/iie/news.asp?Newsid=189>, 15 June 2004. The task force was closed down in December 2003

¹⁷¹ Source: Laksamana net, Indonesian politics and economics portal, "Lonsum Creditors Approve Restructuring", February 29, http://www.laksamana.net/vnews.cfm?ncat=41&news_id=6718

¹⁷² Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

¹⁷³ Source: 'PT PP London Sumatra Indonesia Tbk. and Citicorp', Jan Willem van Gelder (Profundo), study on behalf of Rainforest Action Network, September 2001, <http://www.profundo.nl/publicaties/lonsum1.html>, 15 June 2004

As said, according to BWI's inside LonSum sources, the palm oil company still owed Citibank 99 million dollars at the end of 2003. This would be almost 40% of LonSum's total debt of \$260 million. BWI claims that if a bank holds such a large portion of a company's outstanding debt, it must have significant control over the company. This would still make Citibank co-responsible for LonSum's policies and activities, even if it has decided not to grant any new loans to the palm oil business¹⁷⁴.

Carrying responsibility for LonSum's actions is a great burden. The company has violated national and international laws and codes of ethics so often and so blatantly in the last few years, that any association with this company has a profoundly damaging effect on a bank.

To give some examples of LonSum's misconduct of the last few years:

- In 1996 LonSum decided to expand its business by clearing forest areas in East Borneo. 31,000 Hectares of the Dayak Benuak tribe's forests were bulldozed and burnt. The Dayak Benuak people had no choice but to accept the clearing of their land. People that protested against the activities of LonSum were arrested by the police or were forced to accept compensation money for their destroyed property. Protests in the Dayak Benuak area continued for years, and in 1999 a number of police officers were hired by LonSum to attack one of the local villages and arrest eight of the protestors. This is a clear violation of these native people's internationally established human rights.
- In South Celebes, similar human rights violations occurred just one year ago, in 2003. During the 80s and 90s LonSum had cleared thousands of hectares of forest for rubber plantations in an area where people belonging to the Kayang tribe had lived for generations. Land clearing continued in the new millennium. In the Bonto Mangiring district, traditional plantations of the local villagers were cut down by LonSum, and therefore the villagers missed two harvests. In March 2003, LonSum employees got into a conflict with people from the village of Lapparayya, and set five of their houses on fire. Gunshots were fired at the local people, and two local villagers were hit. The police was present when this happened but did not intervene.
- On the 28th of May 2003, policemen were seen to have lunch with LonSum employees in the Bonto Mangiring district. The next day, 4 local people that were known to be opposed to LonSum's operations in the area were arrested.
- On July 21st 2003 the conflict escalated when close to 320 policemen from the Bulukumba, Bantaeng and Sinjai Resort Police (Polres) violently oppressed a demonstration by the traditional Kajang people, who were protesting against LonSum because the company confiscated their ancestral land. On this day, 4 people died, 20 got injured and dozens of people were arrested. The number of actual victims may have been higher, because many injured people hid from the police in nearby forests, and the people that were arrested did not receive proper healthcare. Apart

¹⁷⁴ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

- from illegally arresting and detaining people, Polres also conducted illegal house searches and engaged in illegal investigation methods.
- The events of July 21st were investigated by the National Commission on Human Rights. The Commission found that the local people's human rights were clearly violated, and made a list of policemen that should be brought to trial to receive a fair sanction for their role in the conflict¹⁷⁵.

Although Citibank has not given any new credit to LonSum since 1997, it is still one of the main banks that LonSum owes money to. Citibank is actively trying to get its money back from the Indonesian palm oil company up till this very date. As long as the link between Citibank and LonSum exists, NGO's like Business Watch Indonesia think that Citigroup should use all its power to stop LonSum from doing any more harm to the Indonesian people and the rainforest on which their lives depend.

Citigroup's own reaction to the Indonesian palm oil issue is as follows:

"In 1994, Citibank financed the acquisition of LonSum by Napan Group after conducting a full due diligence. At the time, LonSum had established plantations in Sumatra and Java, and had not yet started any expansion. LonSum started expanding and opening new plantations in Kalimantan in 1996 not financed by Citigroup. A different financial services institution and a new syndication for LonSum's expansion refinanced LonSum's acquisition. Citibank did not take part in either of these two syndications. LonSum has defaulted on their outstanding obligation to Citibank and we are in discussion with their financial advisors. Other than trying to collect our debts, Citigroup has not done any new business with that company"¹⁷⁶.

This statement makes it seem that the only financial transaction Citigroup was involved in was the 1994 loan. This was indeed the only direct financing arrangement Citigroup made with LonSum: the subsequent transactions were no loans or investments, but merely facilitating services. The sentence "Citigroup has not done any new business with that company", however, does seem misleading.

It is a difficult discussion whether all types of financial services imply a responsibility of Citigroup for the conduct of LonSum. The safest conclusion would be that Citigroup only carried responsibility for LonSum's activities that were financed through the 1994 loan. At that time, the Group did not have such strict environmental and social criteria as it has today, so the financing of LonSum most probably was not a breach of its own CSR commitments.

¹⁷⁵ Source: BWI, 'The Involvement of Citigroup through London Sumatra Indonesia in the case of Forest destructions, Ecology destructions and Human Rights violations : A Case Study of Indonesia. A REVISED VERSION', January 2004, p. 10

¹⁷⁶ Source: Citigroup website, <http://www.citibank.com/citigroup/citizen/environment/data/questions.htm>, 16 September 2003

In conclusion, Citigroup has not done anything illegal in its relation with LonSum, and it has probably not violated its own commitments. But the fact remains that as the single biggest holder of LonSum debt, Citigroup can try to influence LonSum's behaviour, and it should not hesitate to pick up this responsibility, even today.

2.6: CSR policy and practice in Indonesia: Conclusion and recommendations

In general, Citigroup's corporate strategy and behaviour in Indonesia can be judged positively. The Group offers good services to consumers and a good working environment to employees. The Citibank Peka initiative makes a positive contribution to Indonesian society through education and microfinance programs, and does not display any serious flaws.

As to the four issue areas that are of special importance in Indonesia (corruption, privatisation, labour rights and the environment), no serious violations of basic CSR standards have been found, except for one, which concerns labour rights. Although the evidence gathered by BWI does not give us exclusive proof, it suggests that at least some workers felt they were denied the right to form a labour union by local management. The right to organise as workers is guaranteed by the UN Declaration on Human Rights and by the internationally supported ILO Conventions, as well as by local regulations around the world. Although Citigroup does not explicitly commit itself to the ILO Conventions nor to the UN Declaration, it is expected that the Group will respect such basic labour standards in all its business units.

Citigroup Headquarters carry the ultimate responsibility for the implementation of national and international laws, regulations and standards, including in Indonesia. At a lower level, management of the Asia Pacific Group is responsible for activities in Indonesia. If Indonesian managers do not respect basic labour rights, there should be some internal mechanism within the Group to take corrective measures. It seems there is no such mechanism within Citigroup, and if there is, it is not part of the standard Corporate Social Responsibility policy which is known to the public. The Code of Conduct only specifies the obligations of employees, not their rights. It does say that Citigroup "expects [its] businesses, employees and other representatives to comply fully with appropriate laws [...]" and that "[Citigroup] is committed to fair employment practices". This alone should be enough to guarantee workers their right to form a labour union. If there is indeed a problem in Indonesia regarding the right to form a union, it should be immediately addressed.

As to the remaining issues, some brief recommendations will do. In the area of corruption, more transparency about Citigroup's business contacts in Indonesia would be appreciated. In this case too, local regulations about privacy, including the Banking Confidentiality Law, should be respected. A problem that may arise is that Citigroup's internal standards on this matter, like the Privacy Promise for Consumers, could turn out to be stricter than local regulations. In such an event, Citigroup's Code of Conduct says that: "As a general matter,

when there is a difference between internal policies that apply to you or between jurisdictions in which you conduct business, the more restrictive policy will prevail”. This probably also means internal policy prevails over local jurisdiction if the former is more restrictive, because Citigroup expresses in the same paragraph that it wants employees to act “in a manner consistent with the highest ethical standards”.

We at SOMO hope that there will be an internal discussion about Citigroup’s privacy policy in Indonesia, and that the outcome will be that local regulations will prevail over internal policy in this specific matter. In a country where corruption is so pervasive, it is in the public interest that banks provide the necessary information for an open and transparent discussion.

In the area of privatisation, Citigroup could consider that its role as an advisor in the sale of State Owned Enterprises is controversial, and that it brings on certain responsibilities for the success and the effects of the privatisation process. Again, transparency is an important issue: if Citigroup thinks it is doing the right thing by helping to privatise SOEs, it should not hesitate to defend this position to the public in an open, democratic discussion, which takes the interests of business, government, *and* society at large into consideration.

Finally, in the environmental realm, the adoption of the Equator Principles and the GCIB Environmental and Social Risk Management Policy guarantees that Citigroup will not finance unsustainable oil palm or paper and pulp businesses in the future. As said, the involvement with LonSum still poses a moral responsibility for Citigroup to put pressure on this company to end its unsustainable activities, even if Citigroup is no longer directly involved with financing these activities. As long as LonSum has not paid off its debts to Citigroup, the bank can use its economic and political leverage to influence the oil palm company’s environmental policy and practice.

If members from Citigroup or from any other company, organization or institution should have questions or comments regarding the contents of this report, these can be directed at the following address:

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Annex 1: UNEP Statement by Financial Institutions on the Environment & Sustainable Development

As Revised - May 1997

We members of the financial services industry recognize that sustainable development depends upon a positive interaction between economic and social development, and environmental protection, to balance the interests of this and future generations. We further recognize that sustainable development is the collective responsibility of government, business, and individuals. We are committed to working cooperatively with these sectors within the framework of market mechanisms toward common environmental goals.

1. Commitment to Sustainable Development

- 1.1 We regard sustainable development as a fundamental aspect of sound business management.
- 1.2 Believe that sustainable development can best be achieved by allowing markets to work within an appropriate framework of cost-efficient regulations and economic instruments. Governments in all countries have a leadership role in establishing and enforcing long-term common environmental priorities and values.
- 1.3 We regard the financial services sector as an important contributor towards sustainable development, in association with other economic sectors.
- 1.4 We recognize that sustainable development is a corporate commitment and an integral part of our pursuit of good corporate citizenship.

2. Environmental Management and Financial Institutions

- 2.1 We support the precautionary approach to environmental management, which strives to anticipate and prevent potential environmental degradation.
- 2.2 We are committed to complying with local, national, and international environmental regulations applicable to our operations and business services. We will work towards integrating environmental considerations into our operations, asset management, and other business decisions, in all markets.
- 2.3 We recognize that identifying and quantifying environmental risks should be part of the normal process of risk assessment and management, both in domestic and international operations. With regard to our customers, we regard compliance with applicable environmental regulations and the use of sound environmental practices as important factors in demonstrating effective corporate management.
- 2.4 We will endeavor to pursue the best practice in environmental management, including energy efficiency, recycling and waste reduction. We will seek to form business relations with partners, suppliers, and subcontractors who follow similarly high environmental standards.
- 2.5 We intend to update our practices periodically to incorporate relevant developments in environmental management. We encourage the industry to undertake research in these and related areas.
- 2.6 We recognize the need to conduct internal environmental reviews on a periodic basis, and to measure our activities against our environmental goals.
- 2.7 We encourage the financial services sector to develop products and services which will promote environmental protection.

3. Public Awareness and Communication

- 3.1 We recommend that financial institutions develop and publish a statement of their environmental policy and periodically report on the steps they have taken to promote

integration of environmental considerations into their operations.

- 3.2 We will share information with customers, as appropriate, so that they may strengthen their own capacity to reduce environmental risk and promote sustainable development.
- 3.3 We will foster openness and dialogue relating to environmental matters with relevant audiences, including shareholders, employees, customers, governments, and the public.
- 3.4 We ask the United Nations Environment Programme (UNEP) to assist the industry to further the principles and goals of this Statement by providing, within its capacity, relevant information relating to sustainable development.
- 3.5 We will encourage other financial institutions to support this Statement. We are committed to share with them our experiences and knowledge in order to extend best practices.
- 3.6 We will work with UNEP periodically to review the success in implementing this Statement and will revise it as appropriate.

We, the undersigned, endorse the principles set forth in the above statement and will endeavor to ensure that our policies and business actions promote the consideration of the environment and sustainable development.

Source: UNEP-FI website, last consulted on 17 June 2004
<http://unepfi.net/fii/english.htm>

Annex 2: Equator Principles

We will only provide loans directly to projects in the following circumstances:

1. We have categorised the risk of a project in accordance with internal guidelines based upon the environmental and social screening criteria of the IFC as described in the attachment to these Principles (Exhibit I).
2. For all Category A and Category B projects, the borrower has completed an Environmental Assessment (EA), the preparation of which is consistent with the outcome of our categorisation process and addresses to our satisfaction key environmental and social issues identified during the categorisation process.
3. In the context of the business of the project, as applicable, the EA report has addressed:
 - a) Assessment of the baseline environmental and social conditions;
 - b) Requirements under host country laws and regulations, applicable international treaties and agreements;
 - c) Sustainable development and use of renewable natural resources;
 - d) Protection of human health, cultural properties, and biodiversity, including endangered species and sensitive ecosystems;
 - e) Use of dangerous substances;
 - f) Major hazards;
 - g) Occupational health and safety;
 - h) Fire prevention and life safety;
 - i) Socioeconomic impacts;
 - j) Land acquisition and land use;

- k) Involuntary resettlement;
- l) Impacts on indigenous peoples and communities;
- m) Cumulative impacts of existing projects, the proposed project, and anticipated future projects;
- n) Participation of affected parties in the design, review and implementation of the project;
- o) Consideration of feasible environmentally and socially preferable alternatives;
- p) Efficient production, delivery and use of energy;
- q) Pollution prevention and waste minimization, pollution controls (liquid effluents and air emissions) and solid and chemical waste management.

Note: In each case, the EA will have addressed compliance with applicable host country laws, regulations and permits required by the project. Also, reference will have been made to the minimum standards applicable under the World Bank and IFC Pollution Prevention and Abatement Guidelines (Exhibit III) and, for projects located in low and middle income countries as defined by the World Bank Development Indicators Database, the EA will have further taken into account the then applicable IFC Safeguard Policies (Exhibit II). In each case, the EA will have addressed, to our satisfaction, the project's overall compliance with (or justified deviations from) the respective above-referenced Guidelines and Safeguard Policies.

4. For all Category A projects, and as considered appropriate for Category B projects, the borrower or third party expert has prepared an Environmental Management Plan (EMP) which draws on the conclusions of the EA. The EMP has addressed mitigation, action plans, monitoring, management of risk and schedules.

5. For all Category A projects and, as considered appropriate for Category B projects, we are satisfied that the borrower or third party expert has consulted, in a structured and culturally appropriate way, with project affected groups, including indigenous peoples and local NGOs. The EA, or a summary thereof, has been made available to the public for a reasonable minimum period in local language and in a culturally appropriate manner. The EA and the EMP will take account of such consultations, and for Category A Projects, will be subject to independent expert review.

6. The borrower has covenanted to:

- a) Comply with the EMP in the construction and operation of the project;
- b) Provide regular reports, prepared by in-house staff or third party experts, on compliance with the EMP, and;
- c) Where applicable, decommission the facilities in accordance with an agreed Decommissioning Plan.

7. As necessary, lenders have appointed an independent environmental expert to provide additional monitoring and reporting services.

8. In circumstances where a borrower is not in compliance with its environmental and social covenants, such that any debt financing would be in default, we will engage the borrower in its efforts to seek solutions to bring it back into compliance with its covenants.

9. These principles apply to projects with a total capital cost of \$50 million or more.

The adopting institutions view these principles as a framework for developing individual, internal practices and policies. As with all internal policies, these principles do not create any rights in, or

liability to, any person, public or private. Banks are adopting and implementing these principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank.

Exhibit I: Environmental and Social Screening Process

Exhibit II: IFC Safeguard Policies

Exhibit III: World Bank and IFC Specific Guidelines

Source: Equator Principles website, last consulted on 14 June 2004

<http://www.equator-principles.com/principles.shtml>

Annex 3: The GCIB Environmental and Social Risk Management Policy

Introduction

Protecting natural systems while lifting two billion people out of poverty and advancing economic development are the world's greatest challenges. These three foundations of sustainable development are central to the UN Millennium Goals, to national governments, to companies and to civil society. Citigroup has a broad array of policies and programs addressing environment, poverty and the economy. In 2004 we announced a new set of policies and programs focused on sustainable development. In 2003 we announced a new set of policies and programs focused on sustainable development.

New Initiatives

1. High Caution Zones

Consistent with its responsibilities under and the requirements of the Equator Principles and led by its project finance business, Citigroup will carefully evaluate requests for project finance loans where the borrower's proposed use of proceeds would directly fund activities that Citigroup determines could adversely impact a critical natural habitat.

Citigroup will ensure that the appropriate Citigroup bankers throughout the world are aware of and alert to this new Equator-based approach. Citigroup will periodically engage with various stakeholders and evaluate its experience with these policies in a year with stakeholders and report annually in our Corporate Citizenship Report.

Citigroup will not finance any project or provide general corporate loans to any project (where the use of proceeds is known) if the project or use of proceeds is located within critical natural habitats, unless the sponsor or borrower, as appropriate, has demonstrated to Citigroup's satisfaction:

- The project sponsors have considered economic and technically feasible alternatives to avoid such areas and have addressed these issues in the publicly available EA.
- The project will not significantly degrade or convert the critical natural habitat;
- Project management has adequate capacity and willingness to ensure biodiversity protection and respect for the rights of indigenous communities whose livelihoods or cultural integrity could be adversely impacted;

- Indigenous peoples impacted by the project, whether directly or by induced impact, have the opportunity and, if needed, culturally appropriate representation, and have access to the information to engage in informed participation;
- The governmental authorities at the local, regional or national level have provided mechanisms for the affected communities to be represented or consulted, and international and local laws have been upheld; and
- An Environmental Impact Assessment has been prepared that takes into account such consultations and is publicly available.

Categorical Exclusions

In accordance with the Equator Principles, Citigroup will follow International Finance Corporation Safeguards as in effect at the time Citigroup becomes engaged in a project, from time to time including the following:

- Citigroup will not finance commercial logging operations or the purchase of logging equipment for use in primary tropical moist forest.
- Citigroup will finance only preservation and light, nonextractive use of forest resources in forest areas of high ecological value.
- Citigroup will finance plantations only on nonforested areas (including previously planted areas) or on heavily degraded forestland.
- Citigroup will not finance projects that contravene any relevant international environmental agreement which has been enacted into the law of, or otherwise has the force of law in, the country in which the project is located.

2. Illegal Logging

Citigroup recognizes that illegal logging is increasingly a threat to forests worldwide. We appreciate that forests provide humanity with precious natural resources. As expressed in numerous international forums including the G8, The UN Forum on Forests and the World Summit on Sustainable Development, illegal logging is a significant contributor to the degradation and loss of critical forest ecosystems in many regions around the world. Citigroup recognizes the menace to valued ecosystems and forest community livelihoods posed by illegal logging. We recognize that violations of logging laws around the world can have irreparable damage in fragile forest ecological networks where such illegal activity occurs.

Illegal logging causes a number of adverse environmental, economic, and political or social impacts such as depriving national and local governments of related tax revenue, as well as forest owners and local communities of significant revenues and benefits, and acts as a disincentive to sustainable logging. In some countries the corruption associated with illegal logging undermines the rule of law. As evidenced by recently enacted United Nations Security Council sanctions, illegal logging has been associated with civil wars and, is considered a conflict commodity in various battle zones, funding and sustaining violent upheavals.

In this context Citigroup understands illegal logging to take place where timber is harvested in violation of local and national laws intended to stop illegal logging. Illegal logging includes: a) using corrupt means to gain access to forests, b) extraction without permission or from a legally

unauthorized area, c) the cutting of protected species or the extraction of timber in excess of legal limits or in violation of legally approved forest management plans.

Consistent with Citigroup’s Code of Conduct, all employees of the company and its subsidiaries are expected to act in accordance with the highest standards of personal and professional integrity in all aspects of their employment, and to comply with all applicable laws, regulations and company policies. As such, we will not make loans to companies whom we know to be in violation of local or national laws regarding illegal logging. Citigroup is committed to contributing to the fight against illegal logging and preventing the flow of funds to illegal logging actors. This battle presents new challenges. Successful participation in this fight requires global cooperation by governments, the private sector and civil society.

Citigroup will pursue four policies and programs regarding illegal logging:

- Request Citigroup customers seeking loans related to the extraction or processing of forest resources to make appropriate representations regarding compliance with applicable law. This means that a customer will represent to Citigroup that it will comply with all applicable laws including national and local laws regarding illegal logging. Representation in this context is a binding and documented assurance which, if false, could constitute an event of default. Documentation includes all of the documents required to secure a loan including government authorization as necessary.
- Take the following steps to combat illegal logging as appropriate 1) engage government and industry forums on trade and governance, 2) participate in on-going forums on illegal logging, and 3) support civil society organizations to advocate for forest law enforcement and policy reform.
- Ensure that our businesses and risk management throughout the world are aware of and alert to the issue of illegal logging.
- Deepen our collaboration with knowledgeable stakeholders to strengthen our collective efforts to help prevent illegal logging. Better information on the extent of the problem is a prerequisite to developing practical and effective countermeasures.

3. Investing in Ecologically Sustainable Development

Citigroup has developed a program to invest in sustainable forestry and renewable energy. Citigroup has identified experienced resources to screen and evaluate potential investments in the sustainable forestry and renewable energy industries to ensure that investment opportunities in these two sectors get exposure and an evaluation consistent with all other investments on an ongoing basis.

We see immediate opportunities in three areas:

- A. Investments in independently certified sustainable logging – Citigroup is evaluating specific investment funds dedicated to FSC certified forest products located in emerging markets. Portfolio companies in these funds are committed to low impact logging, maintaining ecosystem function in the forest lands, and marketing branded sustainable product. Their financial success will protect more forests and employ more local people in sustainable commerce. Citigroup will have the capacity to evaluate these investments on an ongoing basis.

- B. Investments in renewable energy – Citigroup will identify experts to evaluate investment funds dedicated to renewable energy technologies such as wind, solar, hydrogen, biomass etc. Investments in these companies reduce the environmental footprint of the energy sector.
- C. Residential Clean Energy Financing - Citigroup will explore existing programs to offer consumer financing for solar panels, residential wind turbines and fuel cells, and other forms of clean energy or energy efficiency fit for residential consumers. Citigroup will offer and market a Fannie Mae energy efficient mortgage product by the first quarter of 2004.

4. Climate Change

The Intergovernmental Panel on Climate Change (IPCC)-a United Nations panel of 2,000 of the world's top climate scientists-agree that human activities are changing the climate. As a global company, Citigroup is taking a proactive stance on this important issue. Citigroup will play a role in the financial sector to reduce greenhouse gas emissions from its own operations, and assist customers to develop in developing financial solutions that help reduce emissions in the value chain and invest in renewable energy.

Citigroup published its first ever report on energy used in 2002 in the over 10,000 buildings it leases or owns globally. This process has engaged 150 employees, and is building Citigroup's understanding and capacity in greenhouse gas emissions reporting and energy use reduction.

Beyond its own direct emissions, Citigroup will report the greenhouse gas emissions from the power sector projects in its project finance portfolio beginning the latter half of 2003 and going forward. This report will occur annually in the Corporate Citizenship report. This is the first time that a private bank will offer such data, which will be produced with methodologies peer reviewed with experts and NGOs. As reporting methodologies become standardized for other sectors, Citigroup may expand the report.

Finally, the above mentioned program to identify investments in renewable energy and energy efficiency will help reduce emissions in Citigroup's chain of activities, by adding customers and business partners with an explicit focus on greenhouse gases and energy efficiency.

Source: website Rainforest Action Network, last consulted on 22 June 2004
http://www.ran.org/ran_campaigns/global_finance/citi_victory_policy.html