



## **STR-RESPONSIBLE SOURCING**

### **DONG ENERGY CODE OF CONDUCT ASSESSMENT REPORT**

#### **OJSC SUEK (SIBERIAN COAL ENERGY COMPANY)**

**APRIL 18, 2011 (REV. JUNE 8, 2011)**

#### **EXECUTIVE SUMMARY**

OJSC SUEK (Siberian Coal Energy Company) is the largest thermal coal producer and energy enterprise in the Russian Federation, and has affiliates and subsidiaries in the Republic of Buryatia, Kemerovo Region, Krasnoyarsk Region, Primorsky Territory, Khabarovsk Territory, the Republic of Khakassia, Zabaykalye Territory. SUEK is one of the coal suppliers to DONG Energy. In December 2010, specific allegations against SUEK as one of DONG Energy's suppliers were published in Danish media related to working conditions at SUEK underground coal mines in the Kemerovo region.

On the basis of the serious accusations raised by Danish media, DONG Energy requested an extraordinary third party assessment of working conditions of its coal supplier SUEK in Russia. Specialized Technology Resources' Responsible Sourcing Division (hereinafter referred to as "STR-RS") was selected by DONG Energy to perform the assessment. The assessment was conducted from March 21, 2011 to March 30, 2011 by a four-person team of social auditors and an external specialist in environmental, health and safety in the mining industry.

The assessment of SUEK mining operations covered SUEK's headquarters in Moscow, SUEK's Kuzbass office in Leninsk-Kuznetsky and three of SUEK's underground mines producing coal for export in the Kemerovo region which is delivered to DONG Energy.

Besides the STR-RS assessment team, two representatives from DONG Energy visited the area and one of the underground coal mines in the period from March 21, 2011 to March 23, 2011 to get an overview of mining industry in Russia and to discuss the issues raised by Danish media.

The methodology used for the assessment consisted of site visits and observation, interviews with employees, management, and stakeholders and documentation review. The assessment team engaged a variety of stakeholders, including the Russian Independent Union of Coal Industry Workers, Kiselevsk territorial division of Russian Independent Union of Coal Industry workers, the South Siberian Division of the Federal Service of Ecological, Technological and Nuclear Control of the Russian Federation (RosTechNadzor, the Russian Federal Mining and Industrial Inspectorate), State Labor Inspectorate in Kemerovo Region, City administration of Leninsk-Kuznetsky, Scientific - Clinical Center for Protection of Health of Coal Mining Workers, Biodiversity Conservation Center, Ingortech (company that installs methane monitoring systems), and the Head of the Coal and Energy Department of the Kemerovo region (via letter).

The standards of measurement used in the assessment included DONG Energy's Code of Conduct for Suppliers, national laws and regulations of the Russian Federation, and ILO Convention 176 concerning Safety and Health in Mines (1995)<sup>1</sup>. Reference standards, used to identify best practices, included the International Finance Corporation (IFC) Performance Standards and the World Bank/IFC EHS Guidelines for Mining.

SUEK's compliance with national and international standards was assessed in the areas of labour conditions, occupational health and safety, and environment. In the course of the assessment, the team observed that SUEK has developed and introduced an integrated management system, in order to ensure compliance of all SUEK enterprises with the international standards in the sphere of quality management, environmental management and management of industrial safety. An ISO 9001 certificate for SUEK; and ISO 14001, OHSAS 18001, and ISO 9001 certificates for SUEK Kuzbass issued by Afnor Certification were provided for review.

The assessment team did not observe any evidence of child labour, forced labour, discrimination, harassment and restrictions to freedom of association practiced in regards of employees. However, a number of issues were discovered in the areas of timekeeping and wage calculation. During the visit to the coal mines, the assessment team observed that regulations accepted and adopted at the level of Headquarters were not understood or fully implemented by the management at the level of the mines. The timekeeping system was found to be not fully transparent which presented limitations in determining compliance with Russian legal regulations and binding collective bargaining agreements. As such, the assessment identified several concerns related to working hours and compensation including provision of insufficient weekly rest to employees, non-compensation of overtime work, insufficient compensation for employees travelling from the surface of the mine to the working area underground.

In the newspaper article published in Danish media in December 2010, SUEK's wage system used for underground workers was criticised for being structured in a way that encourages employees to take major safety risks by, for example, manipulating methane monitoring equipment. Since the wages depend on production volume, the employees may neglect safety procedures that would slow down or suspend operations in order to earn enough money to support themselves and their families.

In January 2011, an amendment to the Federal Industry Agreement on the Coal Industry of the Russian Federation for 2010-2012 was incorporated at the mine level. The Russian Independent Union of Coal Industry Workers reached an agreement with the representatives of coal mining companies in Russia, establishing that the fixed amount of the wage should not be less than 70% and that the variable component of the salary should be not more than 30%. SUEK has signed this collective bargaining agreement. In the course of the assessment, it was observed that the new requirement regarding the components of the wage, aimed to reduce the dependence of employees' wages on the productivity, was not fully implemented throughout the entire company as the compensation method for underground employees practiced at all three mines was still based on production volume (the amount of coal extracted by one team in one month), rather than an hourly rate.

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<sup>1</sup> Russia has not ratified this Convention.

By maintaining a wage system which depends on the production volume, the management is able to potentially motivate employees to continue working under dangerous conditions if the level of methane exceeds permissible limits because termination of the work would result in the loss of productive work for employees, which in turn, affects employees' wages.

During the assessment, it was observed that, from a technical standpoint, SUEK management uses several measures to prevent accidents, including investing in modern methane monitoring systems. However, as pointed out by external experts, it is still possible for employees to interfere with the system in order to prevent it from turning on the alarm and shutting off electricity if the level of methane increases.

There was no evidence detected during the assessment that the management did not allow employees to report on dangerous situations or obliged them to stay at their work places if the level of methane increased. Thus, the only reason why employees would want to tamper with the methane detectors would be the fact that the employees' wages depend on the production volume.

Taking into consideration the dangerous nature of the work and the possibility of interfering with the methane monitoring system, it was recommended to withdraw modify the system of remuneration that completely or partly depends on production volume in line with the requirements of the Federal Industry Agreement on the Coal Industry.

With regards to internal grievance mechanisms, SUEK has an internal grievance procedure in the form of a suggestion box, placed at the entrance to the building (office and other services). At the same time, the grievance procedure does not include registration of complaints at the level of the mines and also does not include a response procedure.

Although there is a formal written procedure that determines SUEK's community engagement strategy, in practice, the activities in this area are limited and does not include identifying and mitigating risks and impacts of the company's operational activities on the surrounding communities. Auditors were not provided with any samples of registered complaints or confirmation of the response procedure.

During the assessment it was observed that SUEK is familiar with local legal requirements on occupational health and safety, protection of the environment and strives to ensure compliance. SUEK has competent personnel responsible for occupational health and safety and environment at the Headquarters, at the regional office (SUEK Kuzbass) and at each mine. The assessment team did not identify any practices that did not conform with the employer's responsibilities under ILO Convention 176, however, a number of minor occupational health and safety concerns were observed during the assessment.

According to documents reviewed, (investment plans for each mine) and as per SUEK management, SUEK has invested over US\$289 million since 2005 in the improvements of occupational and industrial safety at its enterprises. Organizational measures include expenses for medical examination for employees, H&S trainings, and risk assessments, among others. Technical measures cover expenses for ventilation system of the mines, measures against methane and coal dust, fire safety, measures against noise, vibration, excessive temperatures, improvement of lighting at workplaces, and others.

The management also provided data on planned investments in occupational and industrial safety for 2011 for review. SUEK is planning to invest a further US\$45 million) in its underground coal mining enterprises in different regions.

DONG Energy provided SUEK the possibility to review the assessment report and comment on the findings and observations made by STR-RS auditor team.

SUEK had objections with regards to two of the findings on working hours and remuneration.

DONG Energy and STR-RS are in a dialogue with SUEK with regards to interpretation of the associated legal requirements for the two disputed findings and with regards to corrective action plans for the remaining findings.

At this stage, STR-RS has not verified actions which have already been implemented by SUEK since the assessment since the company has not provided supporting documentation or other evidence of implementation. However, a re-audit of the company is planned in order to verify corrective actions and progress at the company within the next 12 months.