The Resource Revenue Transparency Working Group

Background to Recommendations on Mandatory Disclosure of Payments from Canadian Mining Companies to Governments

6/14/2013

Draft Framework for Consultation

The Resource Revenue Transparency Working Group is pleased to share its draft recommendations for a mandatory reporting mechanism that would require Canadian mining companies to disclose their payments to governments, both in Canada and abroad, on a country-by-country and project-by-project basis.

The release of this draft document represents over nine months of collaborative efforts between the Mining Association of Canada, the Prospectors & Developers Association of Canada, Publish What You Pay Canada and the Revenue Watch Institute. Over the coming months, the RRTWG would like to invite stakeholders to submit their written comments and feedback on the draft framework, which will be considered prior to the final endorsement of the framework in November 2013.

The draft framework is accompanied by a background document that provides further information on the Working Group's objectives, a statement of principles that has guided its work, the benefits of improving revenue transparency in Canada, and a synopsis of current disclosure standards. Members of the working group have engaged in significant comparative research of existing disclosure requirements, such as section 1504 of the US Dodd-Frank Act and the EU Transparency and Accounting Directives, with the objective of creating a framework that is well aligned to global developments in mandatory reporting yet suitable for the Canadian context.

For the Working Group it has been crucial that our recommendations reflect not only our objectives as agreed in our July 2012 Memorandum of Understanding, but also the unique Canadian regulatory environment and the needs of stakeholders across the country and internationally. As such, we have engaged proactively with a wide group of stakeholders and experts, including industry members, civil society organizations, government representatives, securities lawyers, tax experts, accountants, academics, and securities regulators from across the country to seek inputs into our framework. Workshops or group discussions on revenue transparency were held in Ottawa, Toronto and Vancouver, and we have consulted with experts and stakeholders on an *ad hoc* basis throughout the process.

The Working Group welcomes the announcement made on June 12th 2013 by the Government of Canada regarding its commitment to implement mandatory disclosure requirements. It is the intention of the Working Group to use the work done to date on this framework to engage with the Federal government on its efforts in this area.

Comments must be submitted by **September 1st 2013**, and can be sent to:

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Background to the Framework

On September 7th 2012, Publish What You Pay Canada, the Revenue Watch Institute, the Mining Association of Canada, and the Prospectors & Developers Association of Canada, announced the official launch of the Extractive Resource Revenue Transparency Working Group ("Working Group"). The Working Group was created in order to collaboratively develop a framework for the mandatory disclosure of payments made to governments by Canadian mining companies, both within Canada and abroad. The goal of the framework is to provide citizens in resource-rich countries with the tools they need to hold governments accountable for natural resource revenues and determine whether their governments collected what was owed, while simultaneously helping companies communicate their contributions to domestic economies and aiding investor analysis.

The Working Group was created following international momentum to improve the transparency of extractive sector payments to governments. In the United States, for example, new securities rules for publicly listed oil, gas and mining companies recently enacted under section 1504 of the 2010 Dodd-Frank Act will require covered companies to report their payments to governments on a country-by-country and project-by-project basis. The European Union is also in the process of implementing similar disclosure requirements through the EU Transparency and Accounting Directives, expected to be finalized in June 2013. Regulations in both the US and EU will complement the existing Extractive Industries Transparency Initiative (EITI), a voluntary regime now adopted by more than 35 resource-rich countries.

Throughout the creation of the framework, members of the Working Group closely examined emerging regulations and standards on the disclosure of payments to governments, including those in the US and EU, as well as the EITI, to ensure alignment while also bearing in mind the unique nature of the Canadian mining industry and its current disclosure requirements. Members of the Working Group are in agreement that alignment across various jurisdictions is necessary, and will be of benefit to governments, industry actors, investors and civil society alike.

The framework's recommendations have been developed by the four members of the Working Group, and are being released at this stage as a complete draft framework aimed at soliciting comments from interested stakeholders. The recommendations are the result of 10 months of collaborative research, dialogue, outreach and negotiation – conducted through extensive consultation with extractive sector companies, investors, regulators, other government officials, academics, accountants, lawyers, and civil society groups across Canada and internationally.

Once the final framework is agreed to by all four members of the Working Group later this year, each organization is committed to engaging with a variety of stakeholders at the federal and provincial levels, in order to promote the implementation of the recommendations set forth in the document. The Working Group welcomes the statement made by Canadian Prime Minister Stephen Harper regarding Canada's commitment to implement mandatory disclosure requirements, and looks forward to inputting into this process.

Statement of Principles

Introduction

In an effort to guide the development of a framework for the disclosure of payments to government by Canadian mining companies, the Resource Revenue Transparency Working Group (RRTWG) has established a statement of principles. This statement provides both overarching principles, as well as issue-specific principles for each particular element of a framework for disclosure by Canadian extractive companies. These principles guided the development of the more detailed policy recommendations outlined in the framework.

Overarching Principles

In the broadest sense, the framework seeks to:

1) Contribute to a process which results in communities, sub-national authorities and national oversight actors having access to the information necessary to hold their governments and decision makers accountable for revenues derived from extractive resource development,
2) Develop a framework that results in project-by-project reporting, on a country-by-country basis, for all levels of government in Canada and abroad;
3) Propose a framework for disclosure that remains broadly consistent with international standards, so as to find alignments, reduce duplication, avoid conflicting reporting requirements between jurisdictions, and seek equivalency with other jurisdictions where possible.

Specific Principles

1. *Definition of Extractive Company*
   While the scope of this framework is mining focused, the participants recognize the overarching goals of the PWYP coalition to expand this reporting to all extractive sectors, to ensure a level playing field and consistency with US and European laws.

2. *Definition of Project*
   With respect to defining a "project," the RRTWG is seeking a definition that:
   a. Provides robust guidance on how to interpret the term 'project' in a manner that meets the rules' objectives;
   b. Offers companies flexibility to apply the term 'project' to different business contexts, as long as this results in citizens having access to the information that will help them hold their governments to account and captures payments made by companies;
   c. Is consistent with the Dodd-Frank definition, which suggests that a 'project' most closely relates to legal agreement(s) that determine the flow of payments between companies and governments, and which prohibits the use of the following definitions of a project:
      i. Project as a country;
      ii. Project as a geological basin;
      iii. Project as a reporting unit;
      iv. Project as material to the company.

3. *Reporting Threshold*

   The RRTWG is seeking a threshold that:

   a. results in the disclosure of payments that are material to citizens;
   b. captures payments made throughout the mining life cycle;
   c. does not create an unreasonable burden on companies;
   d. to the extent possible, reduces the possibility of duplicative reporting.

4. *List of Payment Categories*

   The RRTWG is seeking a list of payment categories that:

   a. captures all payments made to governments above a reasonable minimum threshold;
   b. provides relevant information without creating an unreasonable burden.

5. *Format*

   The RRTWG is seeking disclosure in a format that results in information that is readily available, clearly identified and easily retrievable, with currency and unit of payments that are clearly identified.

6. *Commercial Development*

   The RRTWG is seeking a definition of "commercial development" that refers to all stages of the project lifecycle, i.e., from exploration to closure, and all points of the extractive value chain, i.e., from the point of extraction to the point of export or sale.

7. *Exemptions*

   The RRTWG is looking to:

   a. Prevent uneven reporting and differential treatment of companies;
   b. Discourage states from anti-transparency behaviour.

8. *Verification/Audit requirements*

   The RRTWG is seeking to ensure the accuracy of information being reported, in line with international best practice and accounting standards

9. *Regularity of reporting*

   The RRTWG is seeking to:

   a. Ensure timely reporting on an annual basis;
   b. Ensure companies have adequate time to prepare disclosures.

10. *Schedule of Implementation*

    The RRTWG is seeking to ensure companies have an adequate period of time to implement or adapt existing reporting systems to comply with new disclosure requirements.

11. *Penalties and liability*

    The RRTWG is of the view that penalties and liability should be reasonable and proportionate, while encouraging compliance.

The Development Benefits of Greater Revenue Transparency

Non-renewable natural resources are often among the greatest sources of wealth in resource-rich countries. In over 45 countries, proven subsoil assets are valued above $1,000 per citizen.[1] As such, good management of the revenues generated by their exploration, production and sale is often essential for economic development in these countries.

Natural resource extraction can create jobs, generate business opportunities for direct and indirect suppliers, and contribute to infrastructure development as well as training and skill development. In many countries, regions and communities, significant benefits can accrue via tax and royalty payments which are made from companies to governments and then transformed into public investments like health and education services and physical infrastructure.

Unfortunately, these payments are not always transformed into tangible benefits. Poor governance and mismanagement has, at times, meant that resource revenues have not been spent in the public interest. In some cases, revenues that have been collected by public officials have not made their way into public coffers. Secrecy around flows of funds from the extractive sector have also contributed to mistrust between local citizens, their governments and companies, at times leading to delays or outright conflict.

Accessible, disaggregated information from company financial reports on payments made to governments by extractive sector companies is a vital tool in building public accountability. When country- and project-level information on payments is publicly reported by companies, and this information is easy-to-access, understandable and verified to ensure quality, citizens have a tool to hold their governments to account for the management of these revenues. Provided that government financial information is transparent, this information can also help verify that revenues collected are making their way into government coffers. The benefits of revenue transparency have already been demonstrated in several countries (e.g. Botswana, Guinea, Liberia, Mongolia, Nigeria, and Timor-Leste), where extractive resource revenues have been directed towards domestic investment, improving development outcomes and reducing the need for increased international aid.[2]

Additionally, mandatory payment reporting can improve market stability by providing greater information to investors. Investors often must rely on the country as a unit of account in making comparisons between investment choices. This is especially true in the extractive industries, where assets are necessarily geographically fixed and risks are often high. And yet, under current reporting systems requirements, companies can choose to combine data, making project- and country-specific risk assessments challenging. The World Bank has written that country-by-country reporting offers "a means of assessing exposure to some financial, reputational and political risks," generating information essential to investors, shareholders and other users of financial data.[3] Given the unstable and high-cost environments many resource companies operate in, many investors are keen to see these new measures introduced worldwide in order to assist them in reducing investment risks and raising returns. A recent statement of support for mandatory disclosure requirements and the Extractive Resource Revenue Transparency Working Group, signed by 24 investor institutions in Canada with over $362 billion in assets under

[1] World Bank (2011) *The Changing Wealth of Nations.* Online: http://data.worldbank.org/data-catalog/wealth-of-nations

[2] See RWI 2012 Annual Report at http://www.revenuewatch.org/media/publications/annual-report-2012 and EITI research at http://eiti.org/resources/search?keys=&field_taxonomy_resource_category_tid=70.

[3] Online: http://www.ifrs.org/Current-Projects/IASB-Projects/Extractive-Activities/DPAp10/CL/Documents/CL55.pdf

management, is a testament to this[4]. In addition, investors with over $1 trillion in assets under management have written to the SEC in support of strong US disclosure rules.

Greater revenue transparency can also improve profitability in foreign investments. In some countries, the mismanagement of extractive resource revenues has contributed to increased corruption, wasteful spending, violent conflict, and social and political instability rather than productive investment. These issues have in turn exacerbated inequality and inequitable benefit sharing, and in some cases, can prompt local opposition to extraction sites and instability more generally. Such instability is anathema to a healthy investment climate and can create significant uncertainty in the global mineral supply chain. Improved revenue transparency helps foster trust with local communities and improved governance of natural resources, providing more stable investment and operating environments for companies. An improved business environment increases the reliability of commodity supplies upon which businesses and the public in mineral-importing countries rely.

Last but certainly not least, mandatory payments disclosure can help companies credibly communicate their financial contribution to local and national economies. The full impact of company activities in a country may be poorly understood in certain cases, with claims that companies are not contributing enough. Revenue transparency can help companies better explain how their tax and royalty payments to domestic governments have led to tangible benefits like roads, schools and water facilities.

More and more governments are recognizing the importance of revenue transparency. US and European governments have established mandatory reporting regimes requiring disclosure of publicly listed and some private companies, steps the G8 and G20 communities have welcomed. As of mid-2013, more than 35 countries are formally participating in the Extractive Industries Transparency Initiative. 33 countries have issued EITI reports, accounting for 68 fiscal years of data and over $1 billion in revenues.

Revenue transparency is not a panacea for foreign exchange, debt, and other difficult public finance issues, nor does availability of information automatically lead to improved governance and public accountability. However, without such transparency meaningful evaluation of public finance policy and accountability is not possible.

[4] http://www.pwyp.ca/images/documents/Working_Group/Investor_Statement_RRTWG_revised.pdf

Comparison of Disclosure Requirements in Canada, the United States and Europe

Canada has traditionally been a leader with regards to disclosure requirements for publicly-listed extractive companies, especially within the mining sector. Certainly, Canadian reserves reporting requirements remain a model. However, following the adoption of legislative and regulatory reform in the United States and Europe, Canadian standards for the reporting of key financial disclosures related to payments to governments now lag behind.

Currently, mandatory disclosure of payments in Canada is limited and lacking in detail, and often results in inconsistent, infrequent and mostly forward-looking disclosure on a limited amount of revenue streams. It is often aggregated at a country level which is not detailed enough to be useful to citizens and investors. While a growing number of Canadian mining companies voluntarily disclose project level and country level payments to governments, this is not currently common practice.

New requirements in the US and Europe, in contrast, require more detailed payment information, specifying the type of payment and the government that received the payment, on a disaggregated basis per extractive project, and require the dissemination of such information in an easy-to-use format to aid investors and the public with access to comprehensible, clear information.

In 2010, the United States adopted the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") which, among other financial reforms, includes a requirement in Section 1504, "Disclosure of Resource Extraction Issuers," for any company filing annual reports on a US stock exchange to disclose the payments it makes to the governments of the countries where it operates, on a country-by-country and project-by-project basis. Following two years of extensive consultation with stakeholders, the Securities and Exchange Commission (SEC) released final securities rules to implement Section 1504 in August, 2012. These rules entered into force in November, 2012 and require covered companies to begin reporting on payments as early as 2014, depending on when their fiscal years conclude.

Following the adoption of Dodd-Frank in the US, the European Union adopted legislative proposals to implement similar legislation, to apply mandatory reporting rules to companies listed on EU-regulated exchanges as well as to large, private European companies. The European parliament voted to adopt the legislation in June 2013, which subsequently must be ratified by individual member states.

The adoption of such disclosure requirements complement the Extractive Industry Transparency Initiative (EITI), a voluntary global framework implemented by countries individually in an effort to promote greater transparency and multi-stakeholder dialogue in the extractive sector. In 2013 the EITI International Board, a multi-stakeholder group representing governments, industry and global civil society groups, moved to revise the initiative's minimum reporting standards, including a new requirement to report by project.

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