EUROPEAN COMMISSION

MEMO

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New disclosure requirements for the extractive industry and loggers of primary forests in the Accounting (and Transparency) Directives (Country by Country Reporting) – frequently asked questions

1. What is the objective of the proposed country by country reporting requirement in the Accounting and Transparency Directives?

The new Accounting Directive, repealing the Fourth and Seventh Accounting Directives on Annual and Consolidated Accounts (78/660/EEC and 83/349/EEC) introduces a new obligation for large extractive and logging companies to report the payments they make to governments (the so called country by country reporting-CBCR). Reporting would also be carried out on a project basis, where payments have been attributed to specific projects. The Accounting Directive regulates the information provided in the financial statements of all limited liability companies which are registered in the European Economic Area (EEA).

In order to ensure a level playing field between companies, the same disclosure requirement has been incorporated in the proposal to revise the Transparency Directive (2004/109/EC). This includes all companies which are listed on EU regulated markets even if they are not registered in the EEA and incorporated in a third country.

2. What is the country by country reporting system about?

The Directive introduces a new obligation for listed and large non-listed extractive and logging companies to report all material payments to governments broken down by country and by project, when these payments have been attributed to a specific project. The following types of payments shall be reported:

a) production entitlements
b) taxes levied on the income, production or profits of companies
c) royalties
d) dividends
e) signature, discovery and production bonuses
f) licence fees, rental fees, entry fees and other considerations for licences and/or concessions
g) payments for infrastructure improvements.

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3. What are the main objectives of the new disclosure requirement?

The new disclosure requirement will improve the transparency of payments made to governments all over the world by the extractive and logging industries. Such disclosure will provide civil society in resource-rich countries with the information needed to hold governments to account for any income made through the exploitation of natural resources, and also to promote the adoption of the Extractive Industries Transparency Initiative (EITI) in these same countries. The information disclosed on payments to governments will be publicly available to all stakeholders either through the stock market information repository or the business registry in the country of incorporation (in the same way as financial statements are made available).

4. What is EITI? How does it compare with the Accounting Directive?

The Extractive Industries Transparency Initiative (EITI) is a voluntary initiative with the objective of improving transparency and accountability in countries rich in oil, gas, and mineral resources. Once a host country endorses the initiative, the EITI process is mandatory for all extractive industry operators (including those that are state-owned) operating within that country.

The EU mandatory disclosure requirement will complement the EITI efforts by legally requiring companies registered or listed in the EU to disclose payments to governments along the same lines as EITI. In doing so, the ultimate objective is to contribute to the strengthening of the EITI and to extend its scope to all resource-rich countries.

5. Why did the Commission propose to introduce such a system?

The Commission responded to international developments in this field, in particular the inclusion of a requirement to report payments to governments in the Dodd Frank Act in the United States. In order to enforce this legislation, final implementing rules were adopted on 22 August 2012 by the US Securities Exchange Commission (SEC).

In September 2010, the European Parliament made a request to the European Commission for action in this area. In May 2010, President Barroso publicly expressed the Commission's willingness to propose legislation mandating disclosure requirements for extractive industry companies.

6. What types of companies will be required to disclose payments to governments on a country by country basis?

The Directive introduces a disclosure requirement for payments to governments by listed and large[1] non-listed companies with activities in the extractive industry and the logging of primary forests.[2]

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[1] The Accounting Directive defines a large company as one which exceeds two of the three following criteria: Turnover €40 million; total assets €20 million and employees 250.

[2] Concession-based logging of natural and semi-natural forests.

Both of these industries are often associated with a great source of wealth in resource-rich developing countries. By disclosing payments to governments by the extractive and forestry industries, communities in resource-rich countries will be better informed about government income from licensing such activity and whether the cost to society from losing the natural resource is adequately compensated.

Targeting both listed and large non-listed companies will create a level playing field in the EU. It reflects the fact that large non-listed companies can potentially make significant payments to governments in the countries in which they operate.

7. How will the requirement benefit stakeholders in resource-rich countries?

The reporting of payments to government by the extractive and logging industries will provide civil society with significantly more information on what specifically is paid by EU companies to host governments in exchange for the right to extract the relevant countries' natural resources.

By requiring disclosure of payments at a project level, where those payments had been attributed to a specific project and were material, local communities will have insight into what governments were being paid by EU multinationals for exploiting local oil/gas fields, mineral deposits and forests. This will also allow these communities to better demand that government accounts for how the money had been spent locally. Civil society will be in a position to question whether the contracts entered into between the government and extractive and logging companies had delivered adequate value to society and government.

8. Will such disclosure requirements not harm the competitiveness of EU business?

The text agreed by the European Parliament and the Council maintains the balanced approach proposed by the Commission. EU companies will be required to report payments to governments (e.g. taxes on profits, royalties, bonuses) on a country and project basis where those payments had been attributed to a specific project, and with appropriate thresholds. The threshold below which reporting is not mandatory is set at €100 000 within a financial year, including a single payment as well as a series of related payments.

The reporting on a project basis will be possible on the basis of companies' current reporting structures: the defintion of project covers the operational activities governed by a single contract (or similar legal agreements) that form the basis for payment liabilities with a government. Multiple agreements could nevertheless be considered as one project, provided that they are substantially interconnected.

Given that some extractive industry multi-nationals have already voluntarily decided to disclose some payments to governments, the Commission considers that the effect on the competitiveness of EU extractive and logging companies will be limited. Moreover, the system will be reviewed and modified, as appropriate, within three years after the expiration of the deadline for transposition of the legislation by Member States , taking into account, inter alia, international developments and the competitiveness of EU industry, as well as the scope of the reporting obligations and the modalities of the reporting on a project basis.

In the framework of such review, the Commission may also consider extending the obligation to other industry sectors.

9. How do the EU requirements for country by country reporting differ from the US obligations within the Dodd Frank Act?

The EU disclosure requirements are broadly similar to the US Dodd Frank Act requirements, but go further in two respects. Firstly, the EU logging industry is within the scope of the proposed reporting requirement in addition to the oil, gas and mining industries (in the US only the oil, gas and mining sectors are covered). Secondly, the EU rules will apply to large unlisted companies, as well as listed companies, whereas the US rules are restricted to listed extractive companies only.

10. Does this Directive include conflict minerals disclosure requirement?

No, conflict minerals disclosure requirements are not covered by the Directive. However, according to the Directive, the Commission will have to review the feasibility of introducing such obligations within three years after the expiration of the deadline for transposition of this legislation by the Member States. Such review will consider, inter alia, the introduction of an obligation to carry out due diligence when sourcing minerals, in order to ensure that supply chains have no connection to conflict parties and respect the EITI and OECD recommendations on responsible supply chain management.

On 29 March 2013 the Commission launched a public consultation on a possible EU initiative on responsible sourcing of minerals originating from conflict-affected and high-risk areas. [3]

Moreover, the Commission supports the Kimberley Process (Kimberley Process Certification System Certification - KPCS), which requires participating countries to certify that imported or exported rough diamonds are not conflict diamonds. The Kimberley Process has had considerable success, even though there is still scope for improvement in the system (e.g. improvement in controls in some countries).

11. What about the CBCR requirement recently introduced in the CRD IV (capital requirements) Package?

In March 2013 the EU institutions reached agreement on the CRD IV/CRR Package (see MEMO/13/272). In this context, it was agreed to introduce limited country by country reporting requirements for institutions regulated under the Capital Requirements Directive (CRD IV).

These disclosure requirements are, in a first stage, limited to the names, the number of employees and the turnover in each country of operation. Unless significant negative effects are identified and the disclosure obligations are deferred by delegated act, they will also extend to other information, such as profit or loss before tax, tax on profits or loss, and public subsidies received.

The scope of application of the CBCR requirement agreed under the Accounting Directive is, in contrast, limited to the extractive and logging industries and does not cover institutions regulated under CRD IV.

[3] http://trade.ec.europa.eu/doclib/press/index.cfm?id=882

12. Is the EU undertaking any action to further promote transparency in the context of the G8 activities?

In the final Declaration of the G8 Summit in Deauville of May 2011 G8 governments committed to "*setting in place transparency laws and regulations or to promoting voluntary standards that require or encourage oil, gas, and mining companies to disclose the payments they make to governments*."

The new rules on country by country reporting represent an important step towards delivering on that commitment and helps deepen the G8's special commitment to Africa. Moreover, the EU will continue supporting any action aiming at raising global standards for transparency and fighting corruption, including the promotion of EITI and the progress towards a common global reporting standard.

13. Will companies that already publish a report on the basis of equivalent legal requirements in third countries (e.g. the US) be exempted from the disclosure requirement?

The new rules introduce an "equivalence clause" which would allow companies to publish a report on the basis of the mandatory requirements of a third country, provided that these are considered equivalent to the EU requirement. The power to adopt such equivalence decisions, on the basis of specific criteria concerning, e.g. the content and frequency of the reporting obligation, is delegated to the Commission. This provision aims at eliminating the administrative burden that could stem from double or multiple reporting obligations, whilst safeguarding the objective of the Directive.

More information:

http://ec.europa.eu/internal_market/securities/transparency/index_en.htm

http://ec.europa.eu/internal_market/accounting/sme_accounting/index_en.htm

See also MEMO/13/540 (Accounting Directive) and MEMO/13/544 (Transparency Directive.