

# The Case for Company-by-Company Reporting of Data in the Extractive Industries Transparency Initiative (EITI)

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**June 2009**



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## Acknowledgements

**This report was written by Sefton Darby of S.E.B. Strategy Ltd<sup>1</sup> with assistance from Kristian Lempa and Anna Taylor. Extensive and extremely useful comments on the report were made by Alan Detheridge, Michael Levitsky, and Allaedin Twebti. The report was reviewed by numerous staff and senior management at the Revenue Watch Institute. The author is extremely grateful to the many representatives of extractive industry companies, investors, and civil society groups who agreed to be interviewed for this report.**

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## Executive Summary

This report investigates the issue of whether an aggregated or disaggregated (company-by-company) approach to disclosure should be adopted in countries implementing the Extractive Industries Transparency Initiative (EITI). This question has been a contentious one since the inception of the EITI, in discussions at both the international level and in countries implementing the Initiative. The report examines the weaknesses of arguments that have been made to promote an aggregated standard, and identifies stronger arguments to help civil society groups present disaggregation as the preferable alternative, in discussions with both government and industry officials.

Supporters of aggregated reporting have argued variously that government revenues, not company payments, are the focus of EITI; that citizens will neither be satisfied with nor understand the information disaggregated reporting provides; that disclosure of company payments will not help highlight or curtail corruption; that disaggregation will harm companies' confidentiality and competitive edge; or that it creates political and commercial risks in the hands of an ignorant public or investor community. One by one, author Sefton Darby explores and cogently answers these arguments, to provide background and knowledge for transparency advocates as they advance the cause of disaggregated reporting.

The report finds that not only is there little substance to many of the arguments for aggregating details of company payments to governments, but that a disaggregated approach shows clear benefits to EITI stakeholders. Disaggregated reporting:

- Creates greater transparency of company payments and government revenues.
- Mitigates significant risks to companies which, without disaggregated disclosure, are often falsely perceived to be opaque and/or complicit in corrupt activity.
- Leads to a better-informed market in which all parties are more adequately able to negotiate equitable agreements for the extraction of natural resources.

Disaggregated reporting is becoming the norm in countries implementing the EITI. Almost half of the countries producing EITI reports do so in a disaggregated manner. Companies operating in those countries tend to be neutral on the issue. Only a small number of companies are actively engaged in arguing for aggregated disclosure, and even those companies have accepted disaggregated disclosure in countries where the government has decided to adopt such an approach.

**This report agrees that disaggregated disclosure of information regarding company payments to governments will not provide the public with sufficient information to determine the fairness of licenses and concessions held by companies. While EITI can help feed into processes that examine the quality of extractive deals, and can be used to build greater public understanding of the factors involved, disaggregated reporting in EITI will not alone address all of stakeholders' concerns.**

**However, this report finds that the argument made by some companies – that disaggregated reporting will lead to the disclosure of commercially sensitive data – is largely unfounded. There is no evidence to suggest that any company operating in a country with disaggregated reporting standards has suffered as a result. So long as all companies operating in a country are required to report their payments as part of the EITI process, disaggregation essentially puts all companies on an equal footing. In some cases, it may even help to redress information monopolies used by dominant companies to negotiate uncompetitive deals.**

**The majority of companies opposed to disaggregated reporting take this stance because they believe that such a process will create short-term political risks for them. Their position is based on the false notion that the best way to mitigate risks is not to provide the public with information. Instead, by advancing this argument, some companies are actually creating unnecessary suspicion of and hostility to their operations, which constitutes a significant long-term risk.**

**In a similar vein, some companies believe that investors and the financial analysts who inform those investors are either ignorant of how the industry operates and/or do little to recognise the long-term benefits of mitigating risks through disaggregated reporting. Because of this, some companies are reluctant to support disaggregated disclosure. While this approach of “risk-mitigation-through-ignorance” is still questionable, it is clear that a greater effort could be made to encourage investors to reward long-term risk mitigation efforts by companies.**

### **Recommendations**

**1. Civil society groups involved in lobbying for disaggregated disclosure should focus the majority of their efforts on governments rather than on individual companies. Many companies are neutral on the issue of disaggregation but feel unable to take a lead on the issue. Encouraging governments to mandate disclosure by all companies creates a level playing field for all companies operating in a country.**

**2. Making disaggregated reporting the basic EITI standard will only be achieved by making the majority of EITI countries adopt company-by-company reporting, thereby making it the de facto standard. It will not be achieved by trying to change international EITI policy as set by the EITI Board while some countries and companies are not in favour of such an approach. Civil society groups involved in campaigning on this issue should shift and refocus their advocacy efforts accordingly. Disaggregation will only become the standard by first becoming the norm at the country level.**

**3. More training is required for civil society groups in developing *and* developed countries to help them to understand the various factors which determine the level of payments made by companies to governments.**

**4. More attention needs to be paid to other important factors in how EITI reports are compiled. The issues, for example, of how state-owned companies are involved in the process, or how a government's income from production sharing arrangements is reported, *do* need to be clarified by the International EITI Board and Secretariat in order ensure that EITI remains a credible process. International civil society groups should advocate for these issues to be addressed.**

**5. Countries which decide to adopt a disaggregated reporting process should:**

- **Ensure that adequate resources and time are made available to the independent administrator/auditor hired to compile the EITI report**
- **Allow all companies and government agencies the right to clarify any discrepancies identified during the course of an EITI process before a final report is published.**

**6. More efforts need to be made to ensure that financial analysts and investors properly understand the long-term risk-mitigation benefits that can come from extensive programs of disclosure.**

## 1. Introduction

This report seeks to illuminate of whether countries implementing the Extractive Industries Transparency Initiative (EITI) should adopt a standard that requires company-by-company disclosure of information (a disaggregated approach) or should publish information on revenue flows in a way that does not identify individual companies (an aggregated approach). The question of whether to take an aggregated or disaggregated approach when implementing the EITI has been one of the most contentious debates since the Initiative was launched in 2002. It is the intention of this report to help civil society groups, governments and company participants in EITI programs better understand the debate, and more effectively argue for EITI programs which promote disaggregated disclosure.

While an aggregated EITI program is clearly better than no EITI program at all, disaggregated disclosure:

- Creates greater transparency of company payments and government revenues.
- Mitigates significant risks to companies which, without disaggregated disclosure, are often falsely perceived to be opaque and/or complicit in corrupt activity.
- Leads to a better-informed market in which all parties are more adequately able to negotiate equitable agreements for the extraction of natural resources.

This report was informed by numerous off-the-record conversations with oil, gas, and mining companies, investors, as well as civil society groups.<sup>2</sup> It is not the intention of this report to compare or rank different companies' performance on revenue transparency – the *Promoting Revenue Transparency* report<sup>3</sup> published by Transparency International and the Revenue Watch Institute has already provided an in-depth assessment of company practice in this area.

In the course of researching this report, it was interesting to find that most interviewees saw the issue of aggregation/disaggregation as being either an extremely important one, or not important at all. There appears to be very little middle ground on the issue. It is the view of this report that this issue is important, but even if it is not, the very fact that it remains intensely controversial after more than six years of EITI implementation suggests that it is worthy of closer examination.

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<sup>2</sup> Interviewees are not listed in this report as the interviews were carried out on an off-the-record basis so as to enable people to speak freely and frankly.

<sup>3</sup> See [http://www.transparency.org/policy\\_research/surveys\\_indices/promoting\\_revenue\\_transparency](http://www.transparency.org/policy_research/surveys_indices/promoting_revenue_transparency)

## 2. Background

### *The Extractive Industries Transparency Initiative*

The Extractive Industries Transparency Initiative (EITI)<sup>4</sup> was launched in 2002 with the objective of improving transparency and accountability in countries rich in oil, gas, and mineral resources. Numerous studies have shown that these countries tended to be more corrupt, more susceptible to conflict, and more likely to suffer from low growth, than countries without such resources – the so-called “resource curse” or “paradox of plenty.” Government revenue in most of these countries is characterised by very substantial payments made by a relatively small number of extractive industry companies, and there has often been very little publicly-available information about both company payments and government revenues. The premise of the EITI is that the publication of information about those payments and revenues, and the bringing together of all stakeholders (government, extractive companies, and civil society groups) to manage that process, will directly address some of the tension and mutual suspicion that can contribute to the resource curse.

The most succinct description of what it means to “do EITI” can be found in the “EITI Criteria,” which are as follows:

1. Regular publication of all material oil, gas and mining payments by companies to governments (“payments”) and all material revenues received by governments from oil, gas and mining companies (“revenues”) to a wide audience in a publicly accessible, comprehensive and comprehensible manner.
2. Where such audits do not already exist, payments and revenues are the subject of a credible, independent audit, applying international auditing standards.
3. Payments and revenues are reconciled by a credible, independent administrator, applying international auditing standards and published with an administrator’s opinion regarding that reconciliation including any discrepancies that have been identified.
4. This approach is extended to all companies, including state-owned enterprises.
5. Civil society is actively engaged as a participant in the design, monitoring and evaluation of this process and contributes towards public debate.
6. A public, financially sustainable work plan for all the above is developed by the host government, with assistance from international financial institutions where required, including measurable targets, a timetable for implementation, and an assessment of potential capacity constraints.

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<sup>4</sup> Information on all aspects of the Initiative can be found at [www.eitransparency.org](http://www.eitransparency.org).



The EITI is now a substantial global initiative with an international board consisting of senior representatives from governments, companies, civil society groups, and investors, and is supported by a permanent secretariat based in Oslo and Berlin. At the time of writing, some 30 countries in Latin America, Africa, Europe, and Asia are implementing the Initiative, and of those 30, 11 have published some form of EITI report.

<b>EITI Implementing Countries</b>		
Albania	Azerbaijan**	Burkina Faso
Cameroon*	Central African Republic	Cote d'Ivoire
Democratic Republic of Congo	Equatorial Guinea	Gabon*
Ghana*	Guinea*	Kazakhstan*
Kyrgyz Republic*	Liberia*	Madagascar
Mali	Mauritania*	Mongolia*
Mozambique	Niger	Nigeria*
Norway	Peru	Republic of Congo
Sao Tome e Principe	Sierra Leone	Tanzania
Timor Leste	Yemen	Zambia

Countries marked with an asterisk (\*) have produced one or more EITI reports.

Countries marked with a double asterisk (\*\*) have been validated as "EITI Compliant".

### ***What do aggregation and disaggregation mean?***

Early in the EITI process it became clear that the issue of aggregation/disaggregation was an area of significant disagreement between some of the companies and most of the civil society groups involved in shaping and negotiating EITI policy at the international level. Some companies very clearly indicated that should EITI adopt a disaggregated standard, they would not be able to support the Initiative. Similarly, civil society groups felt that should EITI only require aggregated disclosure, they too would not be able to continue to support it. Because of this, the decision was made that international EITI policy would be neutral on the issue of aggregation/disaggregation, and the decision about which model to adopt would be left to the individual countries implementing the Initiative.

Across all EITI policy documents<sup>5</sup> there is only one explicit reference—in the *EITI Sourcebook* (2005)—to the aggregation/disaggregation issue:

***It is important to note the neutrality of EITI policy on this issue because there have been some instances in which individuals and organisations have referred to EITI as being an aggregated standard, which is simply not the case.***

*Stakeholders will need to agree whether company and host government reports should be made publicly available in an aggregated or a disaggregated manner. The final decision will be made by the host government.*

*Aggregated disclosure would see a single number disclosed for each benefit stream. In this case, particular attention would be required to ensure that the process of aggregation was seen to be trustworthy.*

*Disaggregated disclosure would see the overall number broken down by company and/or license. In this particular case particular attention would be required to ensure that the disaggregated numbers were comparable and meaningful.*

*A principle of the EITI is the recognition that achievement of greater transparency must be set in the context of respect for existing contracts and laws. Particular care should be taken to balance the presumption of disclosure under the EITI with the concerns of companies regarding commercial confidentiality.<sup>6</sup>*

In practice there are two different kinds of aggregation/disaggregation:

- *Aggregation/disaggregation by company*: whether an EITI report identifies contributions made by individual companies, or whether it aggregates information to prevent the identification of contributions made by any specific company.
- *Aggregation/disaggregation by revenue stream*: whether an EITI report provides details of individual revenue streams (e.g., taxes, royalties, bonuses, etc.) or whether it aggregates that information into one figure.

Based on these two variables, four options for the publication of EITI data have emerged, which are summarised in the following chart.

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<sup>5</sup> “EITI Policy” is generally accepted to be the sum-total of the *EITI Principles* (2003), *The EITI Criteria* (2005), *The EITI Sourcebook* (2005), the *EITI Validation Guide* (2006), and a number of *EITI Policy Notes* agreed by the EITI Board from 2007 onwards. All of these documents can be found at <http://www.eitransparency.org/document> and have been recently summarized in the *EITI Rule Book* (2009), which can be found at <http://www.eitransparency.org/document/rules>.

<sup>6</sup> Page 34 of the *EITI Sourcebook*. It is the view of this report that the commercial confidentiality arguments against disaggregated disclosure are not particularly strong. The issue is dealt with in depth on pages 22-26.

<b>Disaggregated by company</b>	<p>Company A paid a total \$X to the government; Company B paid \$Y... etc.</p>	<p>Company A paid \$X in tax, \$Y in royalties, \$Z in bonuses; Company B paid... etc.</p>
<b>Aggregated for all companies</b>	<p>All companies paid a total of \$XXXm</p>	<p>All companies combined paid a total of \$X in tax, \$Y in royalties, and \$Z in bonuses</p>
	<b>Aggregated by revenue stream</b>	<b>Disaggregated by revenue stream</b>

It should be noted that the issue of aggregation/disaggregation refers to the way in which the EITI report is eventually published—not to the actual disclosure of companies and government agencies to the independent administrator or auditor hired to reconcile that data. The administrator is only able to do their job if they are provided with fully disaggregated statements from all reporting entities. Where the report is to be published in an aggregated form the administrator/auditor will be required to maintain the confidentiality of individual company and government agency reports. This is an important point because **producing a disaggregated report does not actually require substantially more time or input from reporting entities.**

***Which countries have adopted which kind of disclosure?***

Of the 30 countries which are implementing the EITI, 11 have produced EITI reports. In the process, two of the above four options for disclosure have been adopted, as summarised in the following chart:

<b>Disaggregated by company</b>			<b>Ghana</b> <b>Guinea</b> <b>Liberia</b> <b>Mongolia</b> <b>Nigeria</b>
	<b>Aggregated for all companies</b>		<b>Azerbaijan</b> <b>Cameroon</b> <b>Gabon</b> <b>Kazakhstan</b> <b>Kyrgyz Republic</b> <b>Mauritania</b>
		<b>Aggregated by revenue stream</b>	<b>Disaggregated by revenue stream</b>

The EITI reports published in Ghana, Guinea, Liberia, Mongolia and Nigeria all identify how much each company has paid in each revenue stream. In Azerbaijan, Cameroon, Gabon, Kazakhstan, the Kyrgyz Republic and Mauritania, the EITI reports identify individual revenue streams but not individual companies.

The adoption of revenue stream disaggregation by every government implementing the EITI demonstrates some presumption in favour of disclosure. Moreover, the fact that five out of the 11 countries that have produced EITI reports have done so in a way in which company figures are disaggregated also demonstrates that it is possible for governments to negotiate with companies in order to adopt a higher disaggregated standard of disclosure.

***What is the policy of extractive industry companies on this issue?***

The scope of EITI programs has varied widely from country to country; EITI policy acts as a framework and provides a minimum standard for disclosure, but leaves a substantial number of issues up to each country to decide. Due to this, it technically does not matter whether an oil or mining company is in favour of aggregation or disaggregation because the decision on the issue will be made by the multi-stakeholder steering group

***Country practice on aggregation/disaggregation has been widely misrepresented, with many organisations stating that only one country (Nigeria) has adopted a disaggregated approach. In reality almost half (five) of the countries that have produced EITI reports have adopted a disaggregated approach.***

in each country, and, where agreement on the issue cannot be achieved, by the government.<sup>7</sup> It is useful, however, to briefly examine the different approaches taken by companies because they influence the debate in a variety of different ways. One can discern five different approaches to the issue of aggregation/disaggregation:

***Different extractive industry companies have adopted different policies on the level of EITI disclosure that they prefer. The different approaches reflect a divergence of views amongst companies about which approach is best for managing political risk in the countries where they operate.***

- *In favour of aggregation:* Some companies have lobbied extensively and consistently in all countries where they operate and where EITI programs are being implemented, for only an aggregated approach to be taken. ExxonMobil's approach to EITI is a good example of this.<sup>8</sup>
- *Leaning towards aggregation:* Many companies have a policy of following whatever is agreed-upon by the stakeholder group or the government, but if pushed will state a preference for aggregated disclosure.
- *Different approaches for different countries:* Some companies decide their policy on a country-by-country basis. BP, for example, has no stated policy on the issue but has chosen to disclose their individual EITI reports in Azerbaijan,<sup>9</sup> even though the main EITI reports there are published in an aggregated form. Anglo American discloses payments to government in the 12 countries which host the company's largest operations.<sup>10</sup>

- *Leaning towards disaggregation:* Companies in this category have a policy of following whatever is agreed by the stakeholder group or the government, but have stated a preference for disaggregated disclosure. Shell's policy on EITI disclosure is a good example of a company with this position:

*Our view is that it is for host governments to decide whether individual or aggregated company payments should be disclosed. But having said that, we start from a position*

<sup>7</sup> In some cases it may be necessary for the government to make regulatory or legislative changes to implement the decisions of the stakeholder group. In some countries, for example, the tax code prohibits the disclosure of an individual company's tax information (regardless of whether it will be published in an aggregated or disaggregated manner) to a third party.

<sup>8</sup> See [http://www.exxonmobil.com/Corporate/community\\_local\\_transparency.aspx](http://www.exxonmobil.com/Corporate/community_local_transparency.aspx), though it should be noted that ExxonMobil does provide disaggregated data in countries which have adopted such an approach (e.g., Nigeria) or where disclosure is a requirement of financing from investors such as the International Finance Corporate (as it was, for example, in Chad).

<sup>9</sup> See pages 50 and 59 of the BP Azerbaijan Sustainability Report at [http://www.bp.com/liveassets/bp\\_internet/bp\\_caspian/bp\\_caspian\\_en/STAGING/local\\_assets/downloads\\_pdfs/s/BP\\_in\\_Azerbaijan\\_Sustainability\\_Report\\_2007\\_en\\_final.pdf](http://www.bp.com/liveassets/bp_internet/bp_caspian/bp_caspian_en/STAGING/local_assets/downloads_pdfs/s/BP_in_Azerbaijan_Sustainability_Report_2007_en_final.pdf).

<sup>10</sup> See page 20 of the Anglo American Report to Society [http://www.investis.com/aa/docs/gr\\_2008\\_04\\_15.pdf](http://www.investis.com/aa/docs/gr_2008_04_15.pdf).

*that individual company payments should be disclosed in each country that is implementing EITI - unless there are good and defensible reasons not to do so.*<sup>11</sup>

- *In favour of disaggregation:* A small number of companies, such as Statoil-Hydro and Talisman Energy, proactively disclose the total level of payments to governments in all countries where they operate, though this information is not broken down by revenue stream.<sup>12</sup>

It is important for stakeholders involved in the EITI process to understand that there is a wide variety of views among companies on this issue. It is also important to realise that while the preceding section outlines the positions taken by some major multi-national extractive industry companies, of increasing importance (and in some cases of greatest importance) are the views held by major state-owned companies which are now investing in operations globally, as well as the views of the local state-owned companies in any given country (should one exist). Civil society groups seeking to encourage disaggregated disclosure need to:

- Publicly praise those companies that take a proactive approach on disclosure and point out that supporting disaggregation has not hurt those companies. There needs to be a positive reward for companies which take such an approach, and civil society groups can have a role in publicly recognising the efforts of such companies.<sup>13</sup>
- Always ask each company in each country what their position is on the issue. Because some larger companies leave decisions on how to manage political and social risks to individual country managers, it is quite possible that *within* any given company there will be people who are both for and against a disaggregated approach.

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<sup>11</sup> Shell's policy can be found at:

[http://www.shell.com/home/content/responsible\\_energy/society/using\\_influence\\_responsibly/payments\\_to\\_governments/our\\_approach/our\\_approach\\_ptg.html](http://www.shell.com/home/content/responsible_energy/society/using_influence_responsibly/payments_to_governments/our_approach/our_approach_ptg.html).

<sup>12</sup> Statoil's policy can be found at:

<http://www.statoilhydro.com/en/EnvironmentSociety/Sustainability/2007/Society/Pages/TransparencyAntiCorruption.aspx> and details of its payments to governments at:

<http://www.statoilhydro.com/en/EnvironmentSociety/Sustainability/2007/Pages/Statistics.aspx>. Talisman's policy on EITI can be found at <http://www.talisman-energy.com/responsibility/transparency/?disclaimer=1> and details of payments to governments can be found on page 34 of its Corporate Social Responsibility Report at:

[http://www.talisman-energy.com/upload/important\\_links/16/06/2007crreport-final.pdf](http://www.talisman-energy.com/upload/important_links/16/06/2007crreport-final.pdf). Some interviewees for this report noted that these companies had only adopted this approach because each had been through a publicly embarrassing situation in which the company was either found to have been paying bribes (Statoil in Iran) or in which there were serious criticisms about how the host government was spending revenues received from the operation (Talisman from its former–now divested–investment in the Sudan). The interesting point here is that both companies have seen disaggregated reporting as a way of guarding against accusations of corruption and/or as a way of ensuring that scrutiny of how oil revenues are spent is focused on governments instead of companies.

<sup>13</sup> One example of how this could be done would be to ensure that the marketing and advocacy which comes out of the Transparency International/Revenue Watch Institute *Promoting Revenue Transparency Project* clearly focuses on praising the high-performing companies identified in the report, not just the laggards.

- Ally themselves with those companies which are in favour of disaggregated disclosure to try to encourage other companies to adopt a more open stance on the issue.

### ***Other important reporting issues***

Two other issues regarding the compilation of EITI reports, although they are not directly related to the question of aggregation or disaggregation, are also worth a brief examination: (i) the role of state-owned companies in the reporting process; and (ii) the way in which the value of government production shares is reported.

#### *The role of state-owned companies in the EITI process*

While the reporting requirements of government agencies and companies involved in the EITI process are reasonably straightforward, special attention needs to be paid to the role of state-owned companies involved in the EITI. These companies mainly exist in the oil and gas sector, although in a few mineral-rich countries the state still directly participates in the sector through a public company. The reason why it is important to focus on the role of such companies is because they display a mixture of often-conflicting private sector and public sector roles, functions and motives. The kinds of issues which typically set these companies apart from their private sector counterparts and which are relevant to the EITI process are:

- In many circumstances the company makes payments to the government both in the usual way that a company would (e.g., through the payment of taxes and royalties) *as well as by acting as a revenue agency* in its own right (e.g., through collecting revenues from other companies).
- In some countries the state-owned company also has non-fiscal regulatory responsibilities regarding the management of the sector. Even where the state-owned company does not have a direct regulatory role, it is not uncommon for the company to have a very substantial influence over sector policy.
- Even where a state-owned company is not the operator of a field or deposit, it is common for that company to have a stake in many or all extractive operations in a country.
- In the case of oil-producing countries, the state-owned company will often be responsible for marketing the government's share of profit oil produced under production sharing contracts.
- State-owned companies will often have non-production related units or subsidiaries which have been created in response to government demands, or to fulfil some sort of non-profit making role (e.g., the provision of public services such as education, healthcare and infrastructure in producing regions).

For these reasons it is important for those involved in designing and running EITI programs to consider the unique reporting requirements of state-owned companies so as to ensure that no material revenue streams are omitted from the EITI process. This report recommends that this issue should be considered in greater depth by the International EITI Board and Secretariat and additional guidance should be developed for how these companies should be included in the EITI reporting process. **In countries where a state-owned company operates, the minimum standard should be that the EITI report clearly differentiates between the revenues generated by a state-owned company as an operator; revenues generated by the company from non-production related activities; and revenues collected by the company on behalf of the government.**

#### *Reporting on production share*

In oil and gas producing countries using production sharing agreements, it is common for a government to receive a certain amount of oil or gas “in-kind” from the operator of a field. Sometimes this production share is sold by the operating company on behalf of the government; sometimes it is sold by the state-owned oil company; and in other countries still, state oil and gas marketing agencies are charged with monetising the government’s production share. The practice of how the value of a production share is reported under EITI has been mixed. In some countries, for example Azerbaijan, the EITI reports simply include details of the physical production share transferred to the government (measured in millions of barrels of oil and thousands of cubic metres of gas). In other reports, such as those from Gabon and Mauritania, the reports provide details of the final cash value of oil and gas sales that were then transferred to the government.

Because of the variety of grades of oil and gas,<sup>14</sup> as well as variable transportation costs, it is not possible to place a value on physical production simply based on the widely quoted prices of oil (most commonly Brent crude and West Texas Intermediate crude). That said, the process of monetising government production share is one in which—if adequate controls are not in place—it is extremely easy for corrupt behaviour to occur. Because of the volatile nature of commodity prices and foreign exchange rates, as well as the relatively large volumes of oil that can be sold in any one transaction, it is relatively easy for an individual to siphon profits off simply by reporting a sale as being made at a time which is slightly different from when the sale actually occurred (and therefore was made at a different commodity price or exchange rate). **Further research into this area is needed in order to make recommendations on how EITI reports should address this issue, though in the interim it is the recommendation of this report that EITI reports should include details of (i) the physical amount of production share received by governments; (ii) average prices for oil and gas sales across the reporting period; and (iii) the total amount of money (in either US dollars or the local currency) realised by the government from oil and gas sales.**

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<sup>14</sup> In some countries it is not unusual for there to be significant differences in the quality of oil extracted from different fields in the country. Different qualities of oil can then be exported either separately or as a blend of different oils.



### 3. Responses to arguments for aggregated disclosure

At both the international level as well as in countries which are implementing EITI, numerous arguments have been made by governments and companies in favour of an aggregated approach. This section of the report outlines some of those arguments and responds to them.

***Argument 1: Focusing on company payments is not the objective of the EITI. The Initiative should concentrate its efforts on the transparency of government revenues.***

Many people interviewed for this report stated that their primary objection to disaggregated reporting was that they believed that it shifted the debate from the accountability and transparency of government revenues (and eventually expenditures) to scrutinising individual companies and whether they were paying “what they should.” As one interviewee put it, “I can only think of one reason for NGOs to want disaggregated payments information and that would be in the hope that it gives them something with which they can attack individual companies.”

Part of this debate is about the history of the EITI itself, and whether it was always intended to be focused primarily on governments, or whether it was always intended to focus on the transparency and accountability of both governments and companies. The earliest agreed statement of EITI policy—the *EITI Principles* (2003)—does place a strong focus on government accountability:

*We affirm that management of natural resource wealth for the benefit of a country’s citizens is in the domain of sovereign governments to be exercised in the interests of their national development.*

*We recognise that a public understanding of government revenues and expenditure over time could help public debate and inform choice of appropriate and realistic options for sustainable development.*

But it should be recognised that from the very start there was also a clear intention for the focus of the initiative to be on both governments and companies. As *EITI Principles* goes on to say:

*We underline the importance of transparency by governments **and companies in the extractive industries** and the need to enhance public financial management and accountability.*

*We are committed to encouraging high standards of transparency and accountability in public life, government operations **and in business**. (Emphasis added)*

The dual focus on governments and companies is deliberate: By scrutinising both sides of the transaction, the EITI processes can hopefully disclose information that will be more credible and will make it harder for one side (whether a government or a company) to deliberately misstate information. What is important to note, however, is that the efforts to promote disaggregated disclosure should be focused on the multi-stakeholder group overseeing the EITI process, and on the government. In some countries, those seeking to promote disaggregation have focused their efforts on companies, despite the fact that it is ultimately within the power of the government to decide what information should be disclosed. Most companies are uncomfortable taking a lead position on issues such as disaggregation: They do not wish to be seen asking for higher or lower standards than other companies. Almost all companies interviewed for this report stated that they would be more comfortable if the decision to disaggregate information were made by a government and if such disclosures were then mandated for all companies operating in a country.

While different stakeholders have different views on whether EITI is or should be focused on governments or companies, the great value of the EITI is that its multi-stakeholder approach and international standards allow all stakeholders to address issues which they may feel unable to address alone. Governments may feel unable to make a positive unilateral move on revenue transparency because of the suspicion in which many governments are held by their citizens. Similarly, as noted above, individual companies may not wish to take a unilateral proactive approach on payment disclosure. In involving all stakeholders, and by mandating the participation of all companies operating in a country, EITI is exactly the right forum through which stakeholders can credibly address sensitive topics such as disaggregated disclosure.

***Organisations involved in lobbying for disaggregated disclosure should focus their efforts on the host government rather than individual companies, who—even if they favour disaggregation—are sometimes reluctant to take a lead position on the issue.***

***Argument 2: Disaggregated information will not give people the information that they want.***

One common argument against disaggregation has been made by those who believe that disaggregated disclosure will not actually provide stakeholders with the information that they want: namely, information that will allow them to determine which companies are paying proportionately more or less than other companies. This debate partially stems from the fact that different countries have adopted a wide variety of EITI programs. The three levels of scrutiny that a country can adopt are:

- *Option 1: How much has been paid?* In this option the independent administrator (normally an audit company) is appointed to gather information from companies and government agencies; to reconcile (but not audit) it; to seek explanations for any discrepancies; and to provide a report with the total amounts which companies say they have paid, and that government says it

has received. All information provided to the administrator is assumed to be correct. This is the approach that has been adopted in the majority of countries which have produced EITI reports.

- *Option 2: Was what should have been paid actually paid?* In this option the independent administrator is asked to not only reconcile company payments and government revenue data, but also to carry out tests on whether that data is correct. These tests may be as simple as looking at whether a consistent commodity price was used in calculating the value of production and production-related taxes such as royalties. The Ghana EITI reports, for example, looked at this issue. It may also require that an auditor be hired to scrutinise company and government accounts to determine whether companies are correctly calculating the payments they should be making and/or whether governments are correctly assessing company tax liability. This is the approach which has been taken in Nigeria’s EITI reports. This option does not address the question of whether a company is paying a “fair” amount of tax, but rather it helps to determine whether the government is correctly assessing (or companies are correctly self-assessing) the payments that are supposed to be made.
- *Option 3: Are companies paying a “fair” amount of tax?* Because of the recent period of substantial rises in commodity prices, many people are asking whether they are receiving a “fair” amount of revenue from the extractive industries. The answer must take into account all of the terms of the existing contract, market conditions, the cost of extraction, etc. Thus far, no EITI implementing country has included this within the scope of their EITI program, though several of them are carrying out reviews of contracts outside the EITI process.

The concern of many companies involved in the EITI process is that those asking for disaggregated publication of company payments hope to use that information to achieve or lobby for the third option of scrutiny outlined above. It is correct that it is extremely difficult to determine the fairness<sup>15</sup> of a contract simply by examining the level of payments that a company makes to a government. This is due to the wide range of factors which influence how much a company will pay to a government. These factors are summarised in the box below.

***Factors influencing the level of revenues derived from an oil or mining operation***

*First mover advantage/taking substantial political risk:* In countries where there has been very little, if any, exploration or production before, a company is taking a greater risk by investing where there is less geological information about the region, and where there may be little sustained history of interaction between the government and major foreign investors. This greater risk will be reflected in a higher return for a company. Providing preferential terms to the “first mover” can sometimes be beneficial for a country because it needs to be able to prove to other potential investors that the country is able to attract and sustain a relationship with investors.

<sup>15</sup> Defining “fairness” is dangerous territory because different stakeholders will have different views on this issue. A reasonably uncontroversial definition would be that a “fair” contract is one which adequately balances the concerns and rewards of the country, the community in which the operation is taking place, and the operator and investors.

*Timing of the project in the commodity price cycle:* Projects will generate different returns for companies and governments based on the expected price of the commodity through the lifetime of the project. Many contracts negotiated in the late-1990s, for example, assumed relatively low commodity prices and thus made provisions for relatively low levels of taxation.

*Geological complexity of the field/deposit:* Mineral deposits and oil and gas fields vary widely in their form and complexity. Some may be very easy to extract, while others (for example, deep offshore oil fields) maybe require very significant technological investment in order to extract them. Different parts of a deposit/field will also be economic or uneconomic to extract at different commodity prices. Geological risk can also continue as a risk after extraction begins. It is common for estimates on how much can be extracted from a field or deposit to change as a company develops a better understanding of geological structure over the course of extraction.

*Quality of the field/deposit:* The quality of oil and gas varies immensely from field to field, and the ultimate sale price is therefore highly variable: light sweet crude (i.e., oil that is easily refined into other products) sells for much higher prices than heavy sour oil (which requires more refining and is often unsuitable for use in certain industries). Similarly, deposits of metals will vary immensely according to how concentrated the metal ore is in the deposit. These differences in the quality of deposits and fields, and hence the value of the oil, gas, mineral or metal, is also dependent upon the proximity of other infrastructure such as smelters and refineries.

*Proximity to markets:* While some high-value extractives (e.g., gold, diamonds, and oil) can economically be transported globally, the value of some products varies greatly according to the proximity of markets. The utilisation of gas, for example, requires either very expensive gas transportation tankers, or a pipeline that delivers the product to local utilities or consumers. In some cases, the absence of a local market for gas associated with oil production leads to the gas being vented or flared instead of commercialised. Similarly, some minerals (e.g., sand, granite) may have such a low value relative to transportation costs that it is only economic to sell the product locally rather than internationally.

*Infrastructure and capital expenditure costs:* Different projects require different levels of investment to extract. Those resources which are onshore and which are close to existing infrastructure (e.g., roads, railways, ports, pipelines) may require relatively little capital expenditure to extract. Others may require the construction of substantial new facilities and infrastructure to extract and transport the commodity. The prices of capital expenditures (e.g., steel for construction) are sometimes highly variable.

*Operating costs:* Different fields or deposits will have different levels of ongoing operating cost according to what stage of production they are at; global prices for materials and labour (which can vary immensely over time); and the efficiency of the operation. Higher operating costs will reduce profit-related tax liabilities.

*Financing arrangements:* How a project is financed by the operator will affect the project's revenue streams. Companies which finance their projects with very high levels of debt relative to equity will obviously have higher project costs (interest payments), which in turn reduce revenues to governments. Where an operator is required to "carry" the cost of state participation in the project (i.e., where the state takes a percentage stake in a project but does not pay for its share of costs), the cost of that carried interest will also be recouped by an operator.

*Stage of the project:* Payments to government will vary drastically according to what phase the project is in. Companies will make very few payments while a project is being developed, even though the company may be very visible (due to construction) during that time. Even after production begins a company will still be recovering the costs which it has incurred in developing the project. It is not uncommon for it to take several years of production before a company begins to make substantial payments to a government.

*Different fiscal terms of a contract:* Some contracts may be structured to make payments very early on in a project (sometimes in the form of signature or production bonuses), but these payments will be offset by lower returns to the government over the lifetime of the project.

*Unexpected events:* It is not uncommon for a project to suffer from unexpected delays in production due to accidents, environmental concerns, security and conflict concerns, natural disasters, etc. In some cases these may simply lead to a temporary shutdown in production; in other cases they may fundamentally impact on overall profitability of the project.

It is important for stakeholders involved in EITI processes to understand all of these factors, so that people are not led to believe that the fairness of a contract can be determined simply by looking at the levels of payments made to government. However, if stakeholders receive training to understand these variables, and if information is disclosed over the course of several years (so that people can see the level of payments at different stages in the project and in different market conditions), it does become possible for stakeholders to develop a better understanding of extractive industry projects.

All of that said, it is important for companies to think at an early stage in each project about how they might proactively address the lack of public understanding of the fiscal regime applied to their operation. A strategy of managing this lack of understanding by declaring that the public are incurably ignorant is no strategy at all. Raising public awareness and understanding *is* difficult, but it has a far greater chance of addressing misunderstandings and the risks that come from that lack of knowledge than not addressing the issues at all.

***Argument 3: Disclosure of individual company payments will not provide information that could be used to identify corruption.***

Across all EITI countries there is often a belief that EITI has an explicit anti-corruption focus, and that corruption will not be able to be identified unless information is published on a company-by-company basis. Whether EITI is an anti-corruption initiative remains contentious in many circles. In the majority of countries the EITI process does not involve a re-auditing of company and government data and thus it will, in most cases, be very difficult for an EITI process to identify individual corrupt payments. Some companies therefore believe that to promote disaggregated reporting promotes unsustainable and unrealistic public expectations of what the EITI process will deliver.

EITI **is not** a forensic anti-corruption initiative – it does not investigate every payment made by every company to every government agency or individual in a country. As with any form of financial reporting, EITI reports aggregate multiple transactions to provide an overall picture of the total payments made by a company (or companies) to government. If stakeholders involved in an EITI process want it to be an overtly forensic anti-corruption process that goes digging for evidence of day-to-day corruption then the key area which they need to negotiate is not whether the final report will be aggregated or disaggregated. Rather, they should focus on ensuring that the terms of reference for the EITI administrator requires that that company carry out a full financial audit of company and government data, and on ensuring that that audit includes a determination of whether taxes and royalties paid to a government are consistent with the physical output of the company (i.e., how much oil, gas, metals, or minerals were actually produced). It is also useful to pay close attention to company costs and to benchmark the operating costs of companies against other companies operating on similar projects around the world. EITI **does not** require such a level of scrutiny by the independent administrator, although some countries (such as Nigeria) have carried out full audits as part of their EITI process.<sup>16</sup>

That said, the total amount of information paid by a company to a government can be used to detect corruption at a macro-level on a company-by-company basis. While Argument 2 (above) notes the variables that will affect the financial return from an oil field or mineral deposit, experts who understand these factors could well use disaggregated data to get a general feel for whether there are any very significant variations between what different companies are paying, and thus determine whether there is a possibility that a company is not paying what it should be paying; that a government is not assessing that company's tax and royalty liabilities correctly; or that the terms of a license were set too generously. Moreover, where there is a state-owned company which is responsible for collecting revenues from other companies, disaggregated reporting might assist in determining whether the state-owned company is passing on the full amount of revenue that it has collected.

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<sup>16</sup> More details on what level of scrutiny is required by the EITI administrator can be found in the *EITI Sourcebook* and *EITI Validation Guide*. At a minimum, the audit company appointed as EITI administrator is required to reconcile company and government data that has already been audited to international standards. The administrator is not required to (and in most EITI countries does not) re-audit the information provided.

Companies and governments which make the argument that EITI may not help to identify individual cases of corruption are right that the level of public expectation for what an EITI process will deliver needs to be carefully managed. Over time EITI can act as an effective corruption *prevention* tool in that it creates a culture in which disclosure and public oversight of company payments and government revenues is considered the norm; but, as noted above, disaggregated disclosure will not inherently allow for the identification of individual corrupt payments. However, the failure to disclose in disaggregated form **does** create an unwarranted public suspicion of companies and government agencies that are not in favour of such a level of disclosure. Such suspicion may be related to perceptions of the relative equity of different company contracts (see above).

Political risk exists, though, regardless of whether all the causes for it are reasonable or rational. Companies and governments would therefore improve their respective positions by addressing the risks rather than arguing the intellectual merits of those whose suspicion of companies and government agencies are helping to increase those risks. Irrespective of whether disaggregated data can be used to determine either the relative equity of different extractive industry operations, or used as an anti-corruption tool, aggregated disclosure creates a public perception of company and government opacity and possible corruption. Disaggregated disclosure may not always address the specific issues being debated, but it certainly removes an unnecessary cause of suspicion toward companies and government agencies.

***Argument 4: Disclosure of individual company payments to government would breach commercial confidentiality terms in contracts/would be commercially disadvantageous to companies.***

Some companies and governments involved in the EITI have argued that publishing disaggregated information would either breach the confidentiality terms in contracts between companies and governments and/or would provide a company's competitors with useful information. For a discussion on what constitutes proprietary data see the box below. In the course of researching this report, almost all interviewees—including those from companies opposed to disaggregation—stated that concerns regarding commercial confidentiality were in reality either extremely minor or non-existent.

It is true that many contracts between governments and companies contain confidentiality clauses. In most countries implementing the EITI, whether they are publishing aggregated or disaggregated reports, all parties have agreed to waive those clauses to allow all sides to disclose information to the independent administrator or auditor appointed to reconcile the information. So long as both sides agree to waive these agreements, there is no other reason why they cannot be waived. Indeed, a country's participation in the EITI is simply not possible without either a voluntary or legal mechanism that allows government agencies and companies to disclose information to third parties.

***What is proprietary information?***

The need to not disclose “proprietary information” is often used by government agencies and companies who do not wish to be involved in the publication of disaggregated payment data, or more commonly, by companies who do not wish to disclose the contracts that they have with governments for the extraction of publicly-owned resources. Proprietary information in its most simple form could be defined as information that a company has ownership of, and is not the property of the wider public or other competitors. This is particularly common when dealing with company trademarks and intellectual property—i.e., a brand or a particular product that a company has invested in so as to either set itself apart from competitors (in the case of trademarks) or in order to develop a business selling a product or service that is unique to that company. In the case of intellectual property a company will argue that, in order to protect its investment in developing a product, it needs to keep key information about that product or service confidential so as to prevent competitors (who have not paid development costs) from copying its product or service. Such an approach is supported in many countries (and in global institutions such as the World Trade Organisation) by laws which protect companies from misuse of its proprietary data, punish counterfeiters, and/or guarantee a company a time-limited monopoly on the manufacture and sale of a product.

In the context of the extractive industries proprietary data might refer to:

*Geological data on the oil or gas field, or mineral deposit.* Companies will often invest very significant sums of money in determining the size and structure of a deposit and how to most economically extract it. In countries where there is little publicly-available geological data, such information will give a company an advantage over other companies seeking to develop operations in neighbouring areas.

*Data related to the cost of extraction and profitability.* The competitive advantage of any company is its ability to pay as little as possible for raw inputs and to extract/refine/transport its products as cheaply and as efficiently as possible. Companies are thus sometimes sensitive about how much information is disclosed regarding their operational costs, how much they pay for the right to extract (i.e., how much they pay in bonuses, taxes, royalties, production shares, etc.), and on the profitability of individual projects. In these circumstances there can be a direct conflict between a company’s desire to withhold as much information as possible about its operations, and the need for public accountability over how public resources are extracted.<sup>17</sup>

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<sup>17</sup> In some circumstances governments have also been persuaded that ensuring the confidentiality of proprietary data is good for the government. If a company can argue that non-disclosure will help it to maximise its profits, and the government then taxes those profits, a government could be persuaded that non-disclosure allows it to maximise revenue. This argument becomes even more complex when a government holds equity in an extractive industry operation in which other partners do not wish to disclose what they perceive to be sensitive data. In these circumstances the government would be conflicted between its role as a partner in the investment, and its responsibility to ensure transparency and accountability in projects exploiting public resources.



Some companies argue that the extractive industries are subject to a disproportionate level of scrutiny and demands for transparency relative to other industries. A clear case can be made for greater scrutiny of these industries because:

- They are charged with efficiently extracting a **publicly-owned** resource.
- They are extracting a non-renewable resource. Greater transparency and scrutiny is necessary because a country rarely gets a second chance at properly exploiting such resources.
- The level of payments are often extremely large and are extremely concentrated (i.e., a small number of companies might provide the majority of government revenue).

Many interviewees noted that the argument that an EITI process reveals confidential information was made largely null and void by:

- The fact that one cannot determine key commercial information (such as profitability) simply by looking at levels of payments to government. There are so many other factors at play (as noted in the box on pages 18-20), that it would be extremely difficult to glean commercially useful information simply by looking at payments to government.
- Substantial amounts of information on contracts between governments and companies, joint production ventures, or on rates of commercial returns on oil fields are already available from companies such as Wood-Mackenzie.
- EITI does not require the disclosure of proprietary data such as geological information or the operational costs and profitability of individual operations. Indeed, in countries where a company is operating more than one mine or oil/gas field, any attempt to derive this data from EITI reports would be rendered impossible by the fact that even disaggregated EITI reports aggregate the payments made by a company across all of its operations.

The only area in which there was some consensus among interviewees that disclosure could reveal commercially sensitive information was in “frontier countries”— i.e., countries that are only just beginning to develop their resources. In countries such as these, early investors have invariably taken significant risks in investing there, have invested significant funds in exploration, and therefore may have negotiated an advantageous deal to compensate them for that risk. Unlike countries with more developed industries, there may in fact be little information already available, and very early investors may be threatened by the disclosure of even small amounts of information. Furthermore, the disclosure of the fiscal regime applied to an early project may undermine a government’s ability to negotiate more advantageous terms with subsequent investors. That said, the need to attract and protect very early investors as well as the government’s own negotiating position needs to be weighed against the political risk of non-disclosure. It is important to note that at present the majority of EITI implementing countries do not fall into this category of being frontier countries.

Even if there is a risk that the disclosure of payments to government data might constitute a competitive risk, EITI, by mandating the participation of all companies operating in a country, exposes all operating

companies to that risk. This process makes companies “mutually vulnerable.” That is, some companies may be exposed to risk, but other companies will benefit from the increased amount of information in the marketplace.

In most countries (and certainly in all OECD countries), companies are required to prepare local annual accounts which must be filed with the government agency responsible for housing information on company registrations and operations (typically the Companies Register or Companies House). The reports filed by companies are normally considered a matter of public record and should in theory be

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***If companies consider their payments to government to be so sensitive as to require aggregation in an EITI process, then by extension they are presumably also against allowing public access to company annual filings. There is therefore a risk that governments and companies which promote aggregated EITI reports may be promoting a process that would disclose less data than is already publicly available.***

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accessible to the public. If a company is listed on that country’s stock exchange then they will also be required to regularly file information on their financial performance. In practice, however, in many developing countries such reports are not easily accessible and it is relatively common for a fee to be charged in order to access a company’s annual filing. There may be differences in how financial information is presented in these reports and EITI reports. Payments to government agencies may be aggregated into a single figure (i.e., one that would not identify individual revenue streams) and the accounts would typically be produced on an accruals rather than a cash basis. But irrespective of such differences, the fundamental point that remains is this: If companies consider their payments to government to be so sensitive as to require aggregation in an EITI process, then by extension they are also presumably in favour of not allowing public access to company annual filings—an argument which would go against the dominant trend of company accountability and disclosure across the world. Indeed, there is some risk that governments and companies which promote an aggregated standard might be seen as suggesting that EITI reports should provide *less* information than is already publicly available (albeit disbursed across multiple company filings).

Several interviewees suggested that the main reason why a small number of companies argue in favour of aggregation on the grounds of commercial confidentiality is because those companies currently possess the greatest amount of information on mineral fields and deposits, and therefore are in the best position to negotiate agreements which are particularly advantageous. Because of this form of market control, disaggregated disclosure may actually make the market more efficient by partially addressing these “information monopolies.” Any market in which one party holds substantially more information than another party will invariably lead to attempts to extract excessive profits. Where large multi-national companies with considerable resources and expertise in negotiating agreements are pitted against under-resourced and under-skilled governments in developing countries, such information

asymmetries pose a great threat to the negotiating ability of the government.<sup>18</sup> Disclosure of levels of payments to government will, on other hand, promote more competitive bids for resources, as well as guard against opaque deals. The exception to this argument would be the disclosure of payments to governments in “frontier countries” (see above). It is also important to note that it is reasonable for companies to expect that proprietary geological data is kept confidential as the company has invested significantly in acquiring that information (and EITI does not require the disclosure of such data anyway).

***Argument 5: Information in the hands of an ignorant public constitutes a serious political risk.***

While some stakeholders have argued that disaggregated disclosure should not take place either because the EITI was never meant to focus on the transparency of companies, or on the grounds of commercial confidentiality, the vast majority of arguments interviewees made for aggregation appear to be based on concerns relating to political risk.

***If a lack of public knowledge and understanding of extractive industry projects constitutes a risk, then making a concerted effort to educate the public is a more sustainable way of managing that risk than simply choosing not to disclose information.***

It is true that there is a public perception that the fairness of extractive industry contracts can be consistently determined simply by looking at the level of payments to government. Because of the variables listed on pages 18-20, it is simply not possible to compare the relative merits of extractive industry projects by looking at payments to government: A mature onshore oil field in a country with well-established infrastructure will invariably pay quite high returns to a government; a very new offshore oil field in a country with little infrastructure will pay considerably less.

Many of the companies interviewed for this study believed, however, that disaggregated information in the hands of a public which is ignorant of these issues will lead to unwarranted criticism of companies and may contribute to demands to renegotiate contracts or nationalise such operations. **It is this argument that lies behind**

**almost all concerns that companies involved in the EITI have with disaggregated reporting.**

Companies are right that in many countries there is a very low level of public understanding of these issues. Their response to the concern, however, seems to be one which is based on an extremely short-term view of political risk. If a lack of public knowledge and understanding constitutes a risk to an operation, then making a concerted effort to educate the public would seem to be a more sustainable way of managing political risk than simply not to provide information that may eventually come to the fore anyway. Changes in governments or government policy can often result in the disclosure of

<sup>18</sup> A company would be able to exploit its access to information on deals negotiated with governments across the world, while an individual government may only have information on deals that were agreed in their own country.

previously confidential contracts, so unless a company is confident that this will never occur, it is ultimately better for them to address political and social risk by promoting disclosure and greater public understanding of the deals they have made with governments.

If a country implementing the EITI decides to take a disaggregated approach it does place a significant responsibility on companies, the government, and particularly on civil society groups to ensure that capacity-building programs are developed to help people to understand the information that will be released.

Interestingly, the experience of disaggregated disclosure in EITI countries thus far seems to suggest that this interpretation of political risk is not necessarily a correct one. Not one company involved in disaggregated payment disclosure has subsequently had its contract cancelled or renegotiated as a result. Around the time of the disclosure of the first EITI report in Nigeria, some accusations were made against companies based on incomplete information. The majority of discrepancies identified in early versions of the report were subsequently reconciled once the audit company compiling the report was able to obtain further information from both companies and government agencies. It is a fair request, therefore, that if a country decides to adopt a disaggregated approach to reporting then:

- Adequate funding should be made available to the administrator/auditor producing the EITI report so that they are able to access information from companies and government agencies that will allow them to adequately investigate any discrepancies between company payment and government revenue figures.
- Adequate time should be given to companies and government agencies to respond to the early findings of an EITI report.
- Reports should not be published in draft form; they should only be published once all parties have had a chance to resolve any discrepancies. The multi-stakeholder group overseeing the EITI process should, however, agree up-front and communicate how much time will be available between the production of a draft report and the eventual publication of a report. Companies and government agencies should have the right of response, but at the same time the amount of time should not be open-ended.

The approach to risk management which relies on limiting information rather than educating stakeholders is an extremely questionable one. Civil society groups and the broader public tend to react to the absence of disaggregated information by assuming the worst: “If the government and companies don’t want to tell us who is paying what to whom, it is because they’re hiding something.” This assumption leads to a slow but steady growth in distrust and resentment of governments and companies, which constitutes a significant long-term risk to both groups.

***Not one company involved in disaggregated payment disclosure has subsequently had its contract cancelled or renegotiated as a result.***

Some interviewees suggested that disaggregation was likely to lead to short-term instability, followed by longer-term stability through the creation of higher levels of public trust in governments and companies. Indeed, a number of interviewees noted that companies that promoted only aggregated disclosure were in fact creating a rod for their own backs: that by not disclosing individual company information they gave civil society groups cause for suspicion and kept them focused on the issue of company non-disclosure rather than on what governments then do with the money. Disaggregated information, by removing that suspicion, transfers the risks associated with tracking spending off of the companies and on to the government.

***Civil society groups and the broader public tend to react to the absence of disaggregated information by assuming the worst.***

***Argument 6: Information in the hands of ignorant investors constitutes an immediate commercial risk.***

Another oft-cited defence for aggregation is that the information would primarily be used by investors and financial analysts in order to more accurately assess the profitability of extractive industry companies. Some companies interviewed felt that, similar to civil

society groups and the broader public, investors did not always understand that payments to governments are only one small element in determining the actual profitability of an operation. As one company put it:

*If we disclose payments which are “small” then we’ll be accused by civil society groups of not paying enough; if we disclose payments which are “large” then investors will declare that we’ve signed a bad deal and will sell our stock.*

Throughout the interviews there was consistent questioning of whether investors in companies take into account efforts by companies to mitigate long-term political risk. If a company discloses payments to governments in an effort to reduce long-term political risk, will it be rewarded by the market for its efforts? The answer of the majority of interviewees, including investors, was that while some investors might eventually factor it in, it is most likely that they would not take such actions into account. There is an inherent disjuncture between the outlook of investors and extractive industry companies. Investors tend to focus on a three- to five-year period in terms of expected returns, and have an even shorter focus when it comes to pricing political risk. Extractive industry operations, on the other hand, are typically 20-plus-year investments which need to manage risk in a very long-term manner.

This argument rests, however, on the same assumption: that the best way to address risk is not to provide information. As several interviewees noted, if a company feels that disclosure is actually mitigating political risk and therefore is adding value to the company, it should explain that to its investors. The investor community has been actively engaged in the EITI, and the *Investor Statement on Transparency in the Extractives Sector*, agreed to by investors representing \$12.3 trillion, clearly shows their understanding of the issue:

*Companies that make legitimate, but undisclosed, payments to governments may be accused of contributing to the conditions under which corruption can thrive. This is a significant business risk, making companies vulnerable to accusations of complicity in corrupt behaviour, impairing their local and global “license to operate,” rendering them vulnerable to local conflict and insecurity, and possibly compromising their long-term commercial prospects in these markets.<sup>19</sup>*

For some time now there has been a natural struggle between companies and their investors with regards to how much information about their operations should be disclosed to the market. Some companies clearly see the EITI and disaggregation of information as yet another phase in that struggle. Companies do have legitimate concerns regarding the cost of constantly providing information, but there is a clear counter-argument that a well-informed market will—unless investors are incurably uneducated—be able to make more accurate decisions with regards to the profitability of a company’s operations. While publication of disaggregated information on payments to governments will not allow investors to immediately discern the prospects for profitability, it will contribute to better informing investors. It is important to note that EITI, while it enjoys the support of investors, was never designed to be a tool for providing them with better market data; its key focus is and must remain the provision of greater transparency and accountability to citizens in developing countries with significant extractive industries.

***Argument 7: Promoting disaggregated approaches will make companies more vulnerable to competition from less scrupulous operators.***

A small number of interviewees stated that one of their concerns with regards to disaggregated reporting is that it would make them more vulnerable to less scrupulous operators, in particular the state-owned companies from middle-income countries (China, Russia, India, Brazil, Malaysia, etc.) which are increasingly investing outside of their home countries. These interviewees’ concern was that if a company was seen to be promoting disaggregated reporting, corrupt local elites might prefer to do business with companies which have no need to operate transparently.

In situations such as these, EITI programs and particularly those which have a disaggregated standard can actually protect more scrupulous investors. If international state-owned companies actually are signing agreements with governments who significantly under-pay a country for its resources, then a transparency program such as the EITI will, in the long term, help to expose those deals, and will ensure that “good” investors are not tarred with the same brush. In these situations companies may not wish to be seen as being at the forefront of promoting a disaggregated approach to reporting, but they certainly would benefit from it. It should also be noted that companies such as Statoil and Talisman – which do disclose information on payments to governments – operate in numerous countries with reputations for high levels of corruption. Disclosure for these companies is clearly not a barrier to investing in corrupt environments. The case of Angola demonstrates that even a country that is widely

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<sup>19</sup> See <http://www.eitransparency.org/supporters/investors>

## THE CASE FOR COMPANY-BY-COMPANY EITI REPORTING

considered to be secretive, and that has refused to join EITI, has been willing to publish some disaggregated data on its revenue. The Ministry of Finance publishes extensive data on how much is being paid to the state each month, breaking revenues down by oil production block and by fiscal line-item (income tax, value of sales of government production share, etc.).

## 4. The benefits of company-by-company reporting

This chapter summarises the reasons why disaggregated reporting can be a beneficial practice. Some of the benefits have already been outlined in the previous chapter.

One of the strongest arguments for disaggregated disclosure is that it prevents “good” companies from being associated with the conduct of “bad” companies. If significant discrepancies are revealed in an aggregated EITI report, and those discrepancies cannot be reasonably explained by the independent auditor hired to compile the report, then every single company contributing data to that report comes under suspicion of having made inappropriate payments. The vast majority of companies operate honestly and within the law, and those companies which do can be exposed to unnecessary risk by an aggregated approach to reporting.

Disaggregated disclosure can also be a pre-emptive panacea to the increasing demands of “resource nationalism,” i.e., where governments seek to nationalise extractive industry companies in the belief that the existing operators are not transferring an adequate proportion of the benefits to the state. Public campaigns against companies (including those inspired by governments) are often only possible in the absence of accurate information. By regularly publishing details of payments to governments, companies are able to defend themselves against accusations that they are not making adequate levels of payments to a country. They can also defend themselves against public frustration with inefficient or wasted government expenditure. In countries where no information is published on the fiscal contribution of companies to government, and where little or no public goods and services are provided, the public will often assume that a government’s failure to provide public goods and services is not because the money has been wasted (as is often the case), but rather because the company is not paying enough. Alternatively they may demand that the company replace the state by providing public goods and services itself. Publication of details of payments to governments is one of the most effective ways of ensuring that citizens demand public goods and services from their governments rather than from companies.

In countries where there is some form of redistribution of extractive industry revenues from the national government to sub-national regional government and communities (such as is found in Peru), disaggregated disclosure is essential for ensuring that the revenue-sharing formula is being applied correctly. It also allows a company to clearly identify the funds that it generates for the communities in the areas where it operates.

As noted in the previous chapter, companies that proactively champion aggregated disclosure are, far from mitigating risks, making themselves the targets of suspicion and hostility. Civil society groups and the public often assume that companies that are against company-by-company disclosure take the position because they have something (corrupt) to hide. Regardless of whether that assumption is correct—and most often it is not—the suspicion is created and *that* constitutes a significant risk to



companies. Political risk is by its nature often illogical, but such risks cannot be addressed simply by arguing the merits; they need to be proactively addressed.

In countries where companies are already required to disclose details of their financial performance through their listing on the stock exchange or their annual company filings, disaggregated reporting under EITI creates no threat at all. Rather, it simply brings together dispersed information and lowers the cost of public access to information already in the public sphere.

## 5. Conclusions and recommendations

In a perfect world, the Extractive Industries Transparency Initiative would not need to exist. The functions carried out by the EITI process should ideally be achieved by a reputable, publicly-funded body that is trusted by all stakeholders and reports to all citizens. EITI exists because in many countries the processes of collecting and comparing information, carrying out audits, and publishing information are not adequately accomplished by the government. In some countries the government does carry out this function but is not trusted to not conceal or manipulate the data for political gain. In countries such as these the EITI acts as an interim building block that can discharge these practices and build the trust between stakeholders required to establish a sustainable, reliable institution charged with collating, where necessary auditing, and publishing high quality data on government revenues.

It is common, in countries where such institutions either do not exist or are not trusted, for the state to be failing in other areas as well. In these circumstances citizens often turn to private companies to carry out the functions of the state. The EITI, and disaggregated disclosure of company information within it, is an extremely effective way of allowing companies to place the burden for development back on governments. Provision of public goods and services by companies may be convenient in the short-term but is dangerous in the long term. Extractive industry companies are not experts in the provision of such goods and services; nor are they guaranteed to continue providing consistent service irrespective of market conditions; nor can their approach to the provision of such goods and services be influenced through the electoral and political process. Disaggregated EITI reporting allows companies to very clearly identify the value of their contribution to the government budget and allows citizens in areas where these companies operate to hold their government to account.

In the debate over whether EITI programs should present aggregated or disaggregated information, the real reasons for each sides' perspective frequently go unacknowledged. Companies and governments sometimes present the debate as one over the dangers of revealing confidential or proprietary data. This issue is largely irrelevant here. Similarly, civil society groups sometimes believe that disaggregated data will allow them to accurately assess the relative equity of different extractive industry operations, or will provide them with information that will allow them to identify corrupt activities. Again, this is simply not the case.

The question of whether to present company payment information in aggregated or disaggregated form is actually a matter of how best to mitigate the political risks and

suspicious that often surround major extractive industry operations. It is the view of this report that any argument over the rationality of these risks or suspicions is largely irrelevant—even if its origin is baseless, the public suspicion is real. Companies and governments that support only aggregated disclosure reinforce a public suspicion that keeps the debate focused on the performance and behaviour of companies rather than on governments. Disaggregated reporting can move the debate forward by addressing this suspicion itself and finally allowing all stakeholders to focus on how extractive industry revenues are spent. Civil society groups advocating for disaggregation need to hone their arguments by better understanding the industry perspective and by focusing their efforts locally, to change the approach to reporting in individual countries, rather than at the international level.

### **Recommendations**

- 1. Civil society groups involved in lobbying for disaggregated disclosure should focus the majority of their efforts on governments rather than on individual companies. Many companies are neutral on the question of disaggregation but feel unable to take a lead on the issue. Encouraging governments to mandate disclosure by all companies offers a level playing field for all companies operating in a country.**
- 2. Disaggregated reporting will only become the basic EITI standard if the majority of EITI countries adopt company-by-company reporting, thereby establishing a de facto standard. It will not be achieved by trying to change international EITI policy as set by the EITI Board, so long as some countries and companies are not in favour of such an approach. Civil society groups involved in campaigning on this issue should shift and refocus their advocacy efforts accordingly. Disaggregation will only become the standard if it first becomes the norm.**
- 3. Civil society groups in both developing *and* developed countries need more training to help them understand the various factors which determine the level of payments made by companies to governments.**
- 4. More attention needs to be paid to other important factors in how EITI reports are compiled. The issues, for example, of how state-owned companies are involved in the process, and how a government's income from production sharing arrangements is reported, *do* need to be clarified by the International EITI Board and Secretariat in order to ensure that EITI remains a credible process. International civil society groups should advocate for these issues to be addressed.**
- 5. Countries which decide to adopt a disaggregated reporting process should:**
  - Ensure that adequate resources and time are made available to the independent administrator/auditor hired to compile the EITI report.**

- **Allow all companies and government agencies the right to clarify any discrepancies identified during the course of an EITI process before a final report is published.**

**6. More efforts need to be made to ensure that financial analysts and investors properly understand the long-term risk-mitigation benefits that can come from extensive programs of disclosure.**