Shareholder Advocacy Forum Comments Re: Disclosure of Payments by Resource Extraction Issuers

March 16, 2020 {Comments Due March 16, 2020}

Vanessa Countryman
Acting Secretary
U.S. Securities and Exchange Commission
100 F Street, NE Washington, DC 20549-1090
Via SEC Internet Submission Form
Re: File No. S7-24-19. Disclosure of Payments by Resource Extraction Issuers
Dear Ms. Countryman,

The Shareholder Advocacy Forum is a nonprofit, nonpartisan organization dedicated to preserving the long-term interests of all shareholders. We are affiliated with Americans for Tax Reform, also a nonprofit, nonpartisan organization focused on lowering taxes and promoting limited government. We appreciate the opportunity granted by the Commission to comment on the proposed Rule 13q-1 and amendment to Form SD to implement Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act – requiring the disclosure of payments administered by resource extraction issuers. Section 13(q) has been included as a statutory mandate in Section 1504 of the Dodd-Frank Act and currently regulates the resource extraction payment process.

Brief History of Section 13(q)

Section 1504 of the Dodd-Frank Act included Section 13(q) to the Securities Exchange Act of 1934[1] – compelling the SEC to promulgate rules that require resource extraction issuers to include an annual report disclosing its payments made to a foreign government or the United States government permitting issuers to engage in the commercial development of oil, natural gas, or minerals. Extraction companies are also required to disclose the total amount and type of payment to the SEC relating to their extraction-related development projects. Lastly, Section 13(q) mandates that issuers provide payment information on an interactive data format called XBRL – Extensible Business Reporting Language. XBRL is an electronic software program used by multinational businesses to compile and standardize data, such as reporting finance and account metrics. Once standardized, the information is widely accepted by domestic regulators and those operating outside the US.[2]

On August 22, 2012 the SEC implemented Rule 13q-1 as mandated by the Dodd-Frank Act and amendments to Form SD (specialized disclosure reports). Subsequently, the previous version of

---

[1] US SEC. "Disclosure of Payments by Resource Extraction Issuers." Securities & Exchange Commission, January 15, 2020. https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers
[2] Adam Hayes. July 2, 2019. "Extensible Business Reporting Language." https://www.investopedia.com/terms/x/xbrl.asp

722 12th St NW # 4
Washington, DC 20005

the 2012 rules were vacated by the U.S. District Court for the District of Columbia on July 2, 2013.[3] In 2016, the Commission adopted its revised version of Rule 13q-1 to provide payment disclosure for resource extraction issuers on June 27, 2016, commonly referred to as the "2016 Rules." The revised rules were overturned by Congress, through a joint resolution under the Congressional Review Act on February 14, 2017. Despite the rejection of the 2016 Rules, the statutory mandate under Section 13(q) of the Exchange Act remains in effect. While the CRA prohibits a regulator from administering a "substantially similar" rule in the future, the Dodd-Frank mandate is still operationally valid, in which case the SEC is compelled to move forward with the current rule.

Objectives of the Proposed Rule

The proposed 13q-1 rule requires the disclosure of payments made by extraction companies. Rooted in increasing transparency and combatting global corruption in the industry, disclosure of revenues by private and state-owned extracting companies is critical to the SEC's pillar functions. Within resource-rich countries, some governments have concealed the revenues and profits generated from resource sales.[4] As the proposed rule suggests, the SEC has thoughtfully tailored its proposal to increase transparency for extraction businesses and shareholders who have an interest in extraction practices.

As noted in Commissioner Elad Roisman's statement regarding the proposed rule, he raised concerns that the SEC is perhaps not the appropriate regulator to draft, issue, or monitor compliance for payments made by extraction businesses:

> "*Some might interpret the failure of the SEC's prior attempts at this rulemaking as a sign that we are not the best agency to carry it out. That said, this is a Dodd-Frank mandate, so I am always happy that the Commission takes its statutory requirements seriously. I do hope that in the future Congress will draft legislation for the agency that directly regulates a particular activity as was not the case here.*"[5]

As required by Title XV's Miscellaneous Provisions of Section 1504 of the Dodd-Frank Act, the proposed rule will allow the Commission to balance Dodd-Frank's mandate and shareholder transparency, without proposing a heavy-handed and overly broad rule that could otherwise create compliance burdens and hinder the industry's ability to function properly. For shareholders, there is a concern that the proposed rule may be overly burdensome and duplicative in nature. When the Commission released a previous version of the proposed rule in 2016, comments filed with the Commission raised similar issues regarding: alternative reporting, the definitions of *control* and *subsidiary*, the definition of *project*, and the not-*de minimus* threshold.

---

[3] Steve Quinlivan. December 20, 2019. "SEC Proposes Rules on Disclosure Payments by Resource Extraction Issuers." http://www.dodd-frank.com/2019/12/20/sec-proposes-rules-on-disclosure-of-payments-by-resource-extraction-issuers/

[4] OECD, 2016, "Corruption in the Extractive Value Chain – Typology or Risks, Mitigation Measures and Incentives." http://www.oecd.org/dev/Corruption-in-the-extractive-value-chain.pdf

[5] US SEC, December 18, 2019, Commissioner Elad L. Roisman, "Statement at Open Meeting on Resource Extraction" *Public Statement.* https://www.sec.gov/news/public-statement/statement-roisman-2019-12-18-resource-extraction

722 12th St NW # 4
Washington, DC 20005

Similar to the 2016 rules, the proposed Rule 13q-1 requires that Form SDs be submitted annually and will include payment information related to all extraction-related commercial development projects.[6]

Form SD will be found exclusively on Form 10–K, Form 20–F, or Form 40–F, all of which are filed with the SEC.[7] Form 10-K is released on an annual basis for companies domiciled in the United States. Form 20-F is filed semi-annually for companies that are not domiciled in the United States or Canada. Form 40-F are required to be filed annually for only Canadian domiciled companies but are subject to filing requirements every three months.[8]

We applaud the Commission for addressing some of the issues raised in the 2016 comments and incorporating several of the suggested reforms in the current proposal.

Alternative Reporting for Foreign Private Issuers

Comments to the 2012 and 2016 rule proposals highlighted a concern regarding alternative reporting standards and an increased compliance burden for foreign-private issuers. According to 17 C.F.R. § 230.405, a foreign private issuer is defined as any issuer which is a foreign government, a national of any foreign country, or a corporation or other organization incorporated or organized under the laws of any foreign country.[9] As a result, foreign extraction companies subject to SEC oversight have had to file duplicative reports in order to comply with payment disclosures for extraction operations in multiple jurisdictions.

Since the statutory mandate of Section 13(q) has existed, the SEC has recommended that affiliated extraction companies subject to SEC oversight prepare reports based on the United States Extractive Industries Transparency Initiative.[10] The Extractive Industries Transparency Initiative is a global standard initiative followed by 53 member nations[11] and "sets a global standard for governments to disclose their revenues from oil, gas, and mining assets, and for companies to report payments made to obtain access to publicly owned resources, as well as other donations."[12]

[6] "Ibid." Securities & Exchange Commission, January 15, 2020.
https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers
[7] "Ibid." Securities & Exchange Commission, January 15, 2020.
https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers
[8] US SEC. Nd. Section 12: Securities and Exchange Act, "Form 40-F". https://www.sec.gov/files/form40-f.pdf
[9] "§ 230.405 Definitions of terms, "Foreign Private Investor," *Code of Federal Regulations*, Title 17: Commodity and Security Changes, Chapter 11: Securities and Exchange Commission, Part 230.
https://www.law.cornell.edu/cfr/text/17/230.405
[10] "Ibid." Securities & Exchange Commission, January 15, 2020.
https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers
[11] "Extractive Industries Transparency Initiative." Nd. https://eiti.org/who-we-are
[12] Julia Simon. November 2, 2017. "U.S. Withdraws from extractive industries anti-corruption effort."
https://www.reuters.com/article/us-usa-eiti/u-s-withdraws-from-extractive-industries-anti-corruption-effort-idUSKBN1D2290

In the previously proposed 2016 rules, the SEC would have allowed issuers to disclose payments made to any foreign jurisdiction if the foreign jurisdiction's disclosure requirements were deemed "substantially similar" to that of the USETI's by the Commission.

The proposed amendments incorporated in the current proposal decrease the compliance burden on extraction businesses that operate domestically and abroad, allowing businesses to prepare and provide a single report. By reducing the compliance burdens, shareholders are not inundated with multiple and duplicative reports to review. Under the current proposal, compliance requirements would be fulfilled if the Commission determines that the foreign reporting regime satisfies the transparency requirements of Section 13(q).

The Shareholder Advocacy Forum is supportive of the Commission's alternative reporting requirement as this would give businesses the option to disclose resource payments on behalf of the company that complies with any foreign jurisdiction, including the USETI. We are encouraged to see the Commission implementing these changes and do not support the recommendation of additional compliance requirements that would create challenges for globally based extraction companies to operate.

Changes to *Control* and *Subsidiary* Definitions for Disclosure to Improve Effectiveness

Under the previously drafted 2016 proposal, disclosure compliance would have required a resource extraction issuer "to disclose information relating to any payment made by the issuer, a subsidiary of the issuer, or an entity under the control."[13] In in the current draft, compliance requirements are comparable to the previous version; however, the current proposal addresses the definition of "control" and "subsidiary" in a move towards much needed clarity.

Originally, "subsidiary" and "control" were defined by Rule 12b-3.444 of the 1934 Securities and Exchange Act and interpreted to mean that disclosure from all parties owned or managed by some portion of the extraction business is required.[14] This presented a challenge for determining whom or which entity (or third party entity) bears the responsibility of reporting the information on behalf of all parties and which entity will be held liable for not reporting.

As a result, the SEC appears to have aligned the definition of "control" with the Generally Accepted Accounting Principles in the current proposal. By aligning the definitions with GAAP, the payment disclosure process will exclude entities or operators that only have a proportionate interest to the company. This will reduce the liability of entities that only play a minor role in the day-to-day operations of the business.

---

[13] US SEC. September 19, 2016. "Disclosure of Payments By Resource Extraction Issuers." *Small Entity Compliance Guide*. https://www.sec.gov/info/smallbus/secg/resource-extraction-small-entity-compliance-guide.htm#_edn1

[14] "§ 240.12b-2 Definitions of terms, "Control, Subsidiary" *Code of Federal Regulations*, Title 17: Commodity and Security Changes, Chapter 11: Securities and Exchange Commission, Part 240. https://www.law.cornell.edu/cfr/text/17/240.12b-2

The proposed rule for Rule 13q-1 will require, "a resource extraction issuer to disclose payments by a subsidiary or an entity under the control of the issuer." [15] The amendment as currently proposed will further supplement these definitional changes and provide additional clarity to the disclosure process. In many cases, extraction businesses have multiple interested parties that are connected to the underlying business's operations but have little-to-no responsibility to report payments. The current proposal provides clarity as to which entity oversees the day-to-day operations and bears responsibility to disclose payments. Such policies will reduce the burden on parties that are not directly involved in the financial reporting process or the over-arching management of daily operations.

Without amending the requirement of disclosure from all parties involved and maintaining the current the definitions of "control" and "subsidiary" from the 1934 Securities and Exchange Act, the Commission would have left in place a barrier that only serves to reduce the efficiency of extraction and industry related businesses. By amending these definitions to comply with those of GAAP, the Commission will further modernize the extraction industry and reduce the likelihood of duplicative disclosures, saving shareholder resources that can be better used on alternative projects.

The Three-Pronged Rule Definition of *Project* Simplifies Base-level Requirements

According to the 2016 proposal, a resource extraction issuer is responsible for disclosing all payments made to a foreign or federal government for every project relating to the commercial development of oil, natural gas, and minerals. The proposed rule appears to have incorporated some of the comments submitted for the 2016 proposal, which provided helpful suggestions for the Commission to consider in the current rule to more clearly define "project" and help minimize confusion within the industry.

As defined in the current proposal the definition of "project" is characterized by using a three-tier definition: "(1) The type of resource being commercially developed; (2) the method of extraction; and (3) the major subnational political jurisdiction where the commercial development of the resource is taking place."[16] The three prongs provide a high level of simplicity for issuers compared to previous versions of the rule.

The first tier will require issuers to disclose whether the project involves the commercial development of oil, natural gas, or another specific mineral. Previously, issuers were required to provide information such as: the quality of the resource or if their operations were engaged in extracting light or heavy crude oil. Tier two requires issuers to acknowledge the process for extraction, through an open pit, a well, or an underground mine. Issuers will not be required to disclose if the extraction business is engaging in vertical or horizontal drilling or involved in hydraulic fracking. The third tier of the definition includes the sub-national political jurisdiction

---

[15] "Ibid." Securities & Exchange Commission, January 15, 2020. https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers

[16] "Ibid." Securities & Exchange Commission, January 15, 2020. https://www.federalregister.gov/documents/2020/01/15/2019-28407/disclosure-of-payments-by-resource-extraction-issuers

722 12th St NW # 4
Washington, DC 20005

where the commercial development of the resource is taking place and requires two sub-tiers of disclosure as it relates to jurisdiction: the country, and the state, province or territory where the project will take place.

The proposed definition will allow the Commission to successfully obtain an appropriate balance that promotes transparency from extraction payments, while reducing the regulatory burden that was anticipated with the previous rule associated with the cost of conducting business.

Exemptions for Conflicts of Law

In the 2016 proposal, there was little relief and limited exemptions for extraction businesses whenever Dodd-Frank's compliance mandate came into direct conflict with a foreign jurisdiction's laws or contract terms. If a conflict arose, the previous proposal would have required issuers to apply to the Commission for exemptive relief, which was determined on a case-by-case basis. The SEC had to spend its limited resources reviewing foreign laws and contracts, leading to delays in extraction projects while increasing business costs or forcing a company to entirely abandon a project. The previous proposal would have discouraged extraction businesses from participating in projects or engaging in offshore operations within particular countries whose laws conflict with the rule's disclosure standards.

With the new proposal, the Commission will provide conditional exemptions from disclosure for extraction issuers whose payment disclosure would otherwise be in conflict with foreign laws. The reduction of qualifying conditions will allow for increased levels of autonomy without being forced to choose between disclosing payments to the SEC or violating foreign laws. Extraction issuers must first provide an explanation to the Commission as why they believe they are eligible for exemptive relief. Under the current proposal issuers are first required to exhaust shareholder resources by first attempting to work with the foreign jurisdiction to exempt themselves from the law in conflict, and comply with the SEC. If relief is not granted from the foreign jurisdiction, the issuer must petition for SEC exemption by providing such admissions on the company's Form SD – including a legal opinion from the company's counsel discussing why the extraction business is unable to provide disclosure – and the location of the foreign jurisdiction, the law preventing disclosure, and its efforts described to exempt themselves from the law-in-conflict.

The Shareholder Advocacy Forum believes the current proposal as drafted will help save Commission and shareholder resources by modernizing the disclosure process and prescribing a clear path to obtain relief from disclosure.

Raising the Not-*De-Minimis* Threshold Promotes Pro-Growth Policies

In the 2016 proposal, the Commission considered a not *de-minimis* threshold or minimum payment disclosure threshold that would have required extraction companies to disclose any payments contributed toward an extraction project above $100,000. This arbitrary threshold would have been regressive in nature, creating multiple reoccurring costs associated with compliance and project completion and would have directly harmed smaller businesses and emerging companies. The current proposal appears to have incorporated some of these concerns raised in previous comments

722 12th St NW # 4
Washington, DC 20005

and the proposed Rule 13q-1 seems to better accommodate all extraction businesses irrespective of their size.

As proposed in the current Rule 13q-1, the Commission has concluded an appropriate not-*de-minimis* threshold to require disclosure for individual payments associated with a project exceeding $750,000. An exception is granted when payments are directed to a foreign government hosting the project or when payments are made directly to the United States Federal Government, in which case payments exceeding $150,000 must be disclosed. The $150,000 threshold does not only refer to project payments, but any payment when the extraction company engages in financial transactions directly with the United States government or with a foreign nation's government, again underscoring the goal of combatting corruption.

By incorporating a $150,000 flat-fee threshold into the proposal both smaller and larger extraction companies have an equal chance to succeed. The not-*de-minimis* thresholds in the current proposal will also help preserve shareholder resources and enable long-term growth within the resource-extraction industry.

We applaud the SEC for its work to protect investors and promote market efficiency, and we thank the Commission for the opportunity to provide feedback on proposed rulemaking measures.

If you should have any questions or comments, please contact James Setterlund by phone at (202) 785-0266, or email at jsetterlund@shareholderadvocacyforum.org or jsetterlund@atr.org.

Sincerely,

James L. Setterlund
Executive Director, Shareholder Advocacy Forum