IASB Discussion Paper *Extractive Activities:*
Intermon Oxfam comments on EFRAG's draft comments letter to the IASB

Madrid, 2 July 2010

Re: Response to EFRAG´s views to Publish What You Pay disclosure proposals.

Intermon Oxfam (Oxfam Spain) welcomes EFRAG's support to PWYP proposals.
The IASB Discussion Paper Extractive Activities contains gaps and weaknesses on disclosure that would undermine them. We won't reiterate here the comments that will be directly addressed to the IASB
However we would like to highlight specific points of EFRAG´s draft comment letter that we consider it would be necessary to clarify, in order to guarantee the purpose and effectiveness of the country by country reporting standard proposed by PWYP

1) ***EFRAG has several concerns regarding whether or not current IFRSs can be applied to extractive activities, albeit with application guidance where necessary, instead of a separate accounting model is developed***

Intermon Oxfam response:

- However, contrary to the above concern, *EFRAG supports the DP proposals that the industry scope leads to similar disclosure requirements and the need to develop a disclosure suite for extractive activities as relevant disclosures for these activities currently do not exist in IFRS.*

- Users IO has spoken to have shown their interest in international accounting standards as the vehicle to introduce the specific disclosure requirements for extractive companies, as it would be the best way to create a level playing field for companies operating in the extractive industry. Users find IFRS´s as the driving force for requirements harmonization, especially for emerging markets.

- In addition, according to Commission staff working document - The Review of the operation of Directive 2004/109/EC (TOD): emerging issues:

The current financial crisis demonstrated that the disclosure of accurate, comprehensive and timely information about securities issuers was essential in order to build sustained investor confidence and allow an informed assessment of their business performance and assets. (……) Only 35% of interviewed stakeholders believe that TOD has enhanced comparability of companies active in the same sector. Most of interviewed stakeholders consider the IFRS´s as being the driving force for an enhanced comparability.

2) ***EFRAG considers that many of the disclosures proposed by the project team already address many of the PWYP objectives. However, where there are divergent needs, the needs of investors and other capital market participants must take precedence.***

We consider that the Discussion Paper contains gaps and weaknesses on disclosure that would undermine the purpose and effectiveness of a country by country reporting standard:

- PWYP proposes the disclosure of production revenues on a country-by country basis whereas DP proposes its disclosure by commodity.

In EFRAG´s own view: *We do not agree that the geographical production revenue is only relevant if the commodity price is subject to local market conditions. If an entity thinks there are geographical risks for its activities, a geographical disclosure of production revenue should be included to be consistent with that.*

We agree with EFRAG that geographical risk leads to the need of country by country disclosure of production revenues. Measurement of these risks, however, can't be let to management criteria in order to protect investors and allow comparability
The extractive industries have unique exposure to material country-specific, tax/regulatory and reputational risks. Exposure to these risks is heightened by the massive capital employed in the extractive industries and the importance of natural resource access and management to the energetic security for consumers.

- PWYP proposes the disclosure of reserve quantities, production quantities and production and development costs on country by country basis. DP also proposes these disclosures, but only if material to the entity. DP also allows exceptions to the reporting requisite.

We think that the current proposal allowing firms to decide whether they report their financial information in a country depending on the importance of the activities of a particular MNC in that country, - "materiality clause" - will reduce comparability of data, a key principle of international standards. Indeed, it would keep accounting information on many countries still aggregated, therefore contributing to maintaining the sector's opacity instead of incentivising transparency Therefore, the reporting standard should require all companies to report for each of the countries where they operate.

The current proposal allows firms to opt out of reporting country-specific data where they feel this would "prejudice the position of the entity" (paragraph 6.37). **We oppose this exemption** because it would remove the protection of a standard reporting requirement, leading to a situation in which the most transparent firms would have to bear the responsibility of justifying to non-transparent governments the reasons why they decided not to make use of this exemption. Thus, companies might face pressure not to report, and legal and operational antagonism if they did. Furthermore, it would deprive investors from getting comparable and consistent data on firms' performance in the different countries in which they operate.
Consequently, there should not be reporting exemptions of any kind nor confidentiality clauses. A uniformly applied IFRS should override restrictions of confidentiality clauses.

3) ***EFRAG considers that many of the proposed disclosures are currently provided elsewhere in the annual report on a voluntary basis.***

We consider that **voluntary disclosure does <u>not</u> create the level playing field that users of financial statements have told us they require**. Although some companies have taken productive voluntary steps to improve their disclosure, capital providers need the audited, consistent and comparable financial data on country by country basis.

4) ***EFRAG considers that the users that they have spoken to have expressed little interest in the additional disclosures proposed.***

We suggest that it would be useful to clarify what is meant by "additional disclosures" beyond those recommended elsewhere in the Discussion Paper. In addition, we think that to fully understand the profile of operations and to enhance transparency in the extractive sector, the financial reporting standard should establish a minimum set of country-specific information that every company should report on. PWYP proposals are meant to be a **fixed** battery of information details needed to get an accurate picture of the companies' performance.

PWYP additional disclosures, compared with those endorsed by the DP project team are:

- Production revenues disaggregation by sales to external customers and transfers to downstream operations.

OECD notes that 70% of world trade is intra-group and, therefore, likely to be subject of illegal practices of transfer pricing abuse or directed to tax heavens. However, not one of those intra-group transactions is broken down in the accounts of the multinationals.

According to various estimations, 50% of global trade passes through a tax heaven and 99% of European biggest enterprises have at least a joint venture in a tax heaven. UK has failed to collect between 3.700 and 13.000 million pounds due to the change of domicile of the offshore companies (The Guardian, February 2009)

The most moderate previsions point out that the illicit capital flight from the developing countries fluctuate from 650 billion and 1.000 billion $ a year, number that exceeds that estimated by the World Bank as necessary to reach the Millennium Development Goals, and multiplies per ten the Official Development Assistance received by those countries. About 60% of this quantity is due to multinational companies that evade benefits throughout abusive practices such as the manipulation of reference prices, and through subsidiaries in tax heavens, in order to avoid paying their taxes.

- The names and locations of each subsidiary and property in each country.

The DP claims that these are already usually available but does not offer proof of it.

- Benefit streams to governments. The significant components of the total benefit streams to government and its agencies should be disclosed on a country-by-country basis. At a minimum, this would include separate disclosure of royalties and taxes paid in cash and in kind (measured in cash equivalents), dividends, bonuses, and licence and concession fees.

In EFRAG´s own view: (Point 98): *In addition, we consider it would be useful to include the following additional disclosures in order to provide useful information related with these costs and their related risks:*
c) Results of operations (revenue, production, exploration, depreciation and amortisation, ***income tax*** *and result)*

We also strongly think there is a wide and explicit support worldwide to this specific disclosure:

- Users we have spoken to have shown a strong interest in extractive industries financial transparency, by country by country reporting.

Investor funds as US Boston Common Asset Management and Storebrand, and Spanish faith-based institutional investors as La Provincia Bética de la Compañia de Jesus lent Intermon Oxfam their voice to ask Spanish oil company, Repsol, in its 2009 and 2010 AGM, for a commitment with payment disclosure to governments (2009), and to support the country by country disclosure in a new IFRS6, 2010. (Find statement attached)

- USA mining company Newmont has publicly supported the Energy Security through Transparency Bill (ESTT), introduced in US Congress in 2009, that would require all mineral companies listed in US SEC to disclose all benefit streams to countries on country by country bases. Newmont has stated “by opening the books to payments, responsibility would shift from extractive firms to local governments, because citizens could hold them accountable once they know how much money they received”

- In 2008, Railpen Investments, the corporate trustee of the various UK railway industry pension funds with an approximate total market value of £14 billion wrote to the IASB noting that: “The proposal for a new international accounting standard, requiring companies to report their payments to government, their reserves, production data and costs, and key assets on a country-by-country basis, are important in order to increase transparency in a high risk industry. We believe that such disclosure is very much part of mainstream financial reporting and will provide investors with better information to judge company exposure in different country contexts"

- Investors supporting the Extractive Industries Transparency Initiative, EITI, (80 institutional investors representing US$ 16 trillion) and those also publicly supporting ESTT are, by doing so, expressing their interest in country by country reporting of benefit streams to government, broke down in payment categories already defined by EITI.

- In May 2010, Calvert Investments published a paper strongly endorsing country-by-country reporting of payments to each country of operation. In this they state that country-specific reporting, "could be used by investors to account for material, country-specific, tax/regulatory, reputational risks and would substantially improve investment decision making regarding the extractive industries sector." This paper argued against leaving decisions on materiality to companies.

The IASB project team states in the DP that they are analyzing PWYP proposals from 2 perspectives:

- cost/benefit analysis
- disclosures consistent with objectives of financial reporting

Therefore we also consider quite relevant highlighting the last EFRAG responses to the DP

5) ***EFRAG considers that their initial assessment of the additional disclosure is therefore that cost of their preparation will not outweigh the benefit of their inclusion in the financial statements***

We agree with EFRAG´s view in this point. 46 mineral companies so far have officially endorsed the Extractive Industry Transparency Initiative. By supporting this Initiative, companies show implicitly their willingness to publish this information. Having a clear understanding of its total tax contribution can enable a business to make better-informed decisions, demonstrate its wider social and economic impact and better monitor and manage tax risk. In PwC's view, *every mining company needs to have this on a regular basis for all its operating markets. It is essential management information and may also be helpful to inform communication and engagement with government and other key stakeholders.*

Some oil, gas and mining companies have taken the lead on voluntary disclosure showing that far from being bad for business, greater openness is likely to improve a company's reputation, credibility and ultimately its profit margin. Some of these preparers we have spoken to have expressed they have not faced any significant cost in gathering the information.

6) ***EFRAG considers that the objective of the financial statements is to provide decision useful information to investors and other capital market participants.***

The constitution of the IFRS Foundation, states that one of its purposes is, *to develop, **in the public interest**, a single set of high quality, understandable, enforceable and globally accepted financial reporting standards …..to help investors, other participants in the world's capital markets and **other users of financial information** make economic decisions*

We think that other users of financial information are also those who consider that public interest includes promoting good governance, the elimination of corruption, the efficient and proper payment of tax and other obligations on a timely basis, the efficient allocation of economic resources, the reduction of systemic risk within economies and the creation of democratically accountable states.

We would finally like to address EFRAG´s attention to the concerns expressed by the EU institutions, regarding country by country disclosure:

- Different EU institutions have voiced support for the development of a new IFRS for the extractive industries. The European Parliament urged, already in 2007, the IASB to "*move beyond voluntary guidelines and support the development of an appropriate accounting standard requiring country-by-country reporting by extractive companies"*

- The European Commission has furthermore recently published a communication on Tax and Development that addresses the importance of genuinely considering the inclusion of country-by-country reporting in the new IFRS for extractive industries

- In 14 June, Foreign Affairs Council conclusions on tax and development stated, *Member States should support ongoing consultation work by the IASB on a country by country reporting requirement in IFRS6 for the extractive sector, and encourage the IASB to look beyond the extractive sector.*

- In November 2008, the European Commission approved and published the Communication from the Commission to the European Parliament and the Council "The raw materials initiative — meeting our critical needs for growth and jobs in Europe" which includes among its recommendations:

B. Promote a sound investment climate that helps increase supply:
Development policy should also promote a clear legal and administrative framework by:
– establishing a level playing field between companies and countries wanting to access raw materials;
– increasing transparency of mining deals and revenues;
– promoting sound taxation systems under which all economic activities – including mining activities – contribute a fair share to the revenues of States

We would also like to thank you this opportunity to provide comments to your draft comment letter to the IASB

Yours sincerely

Irene Milleiro

Director Campaigns and Policy
INTERMON OXFAM