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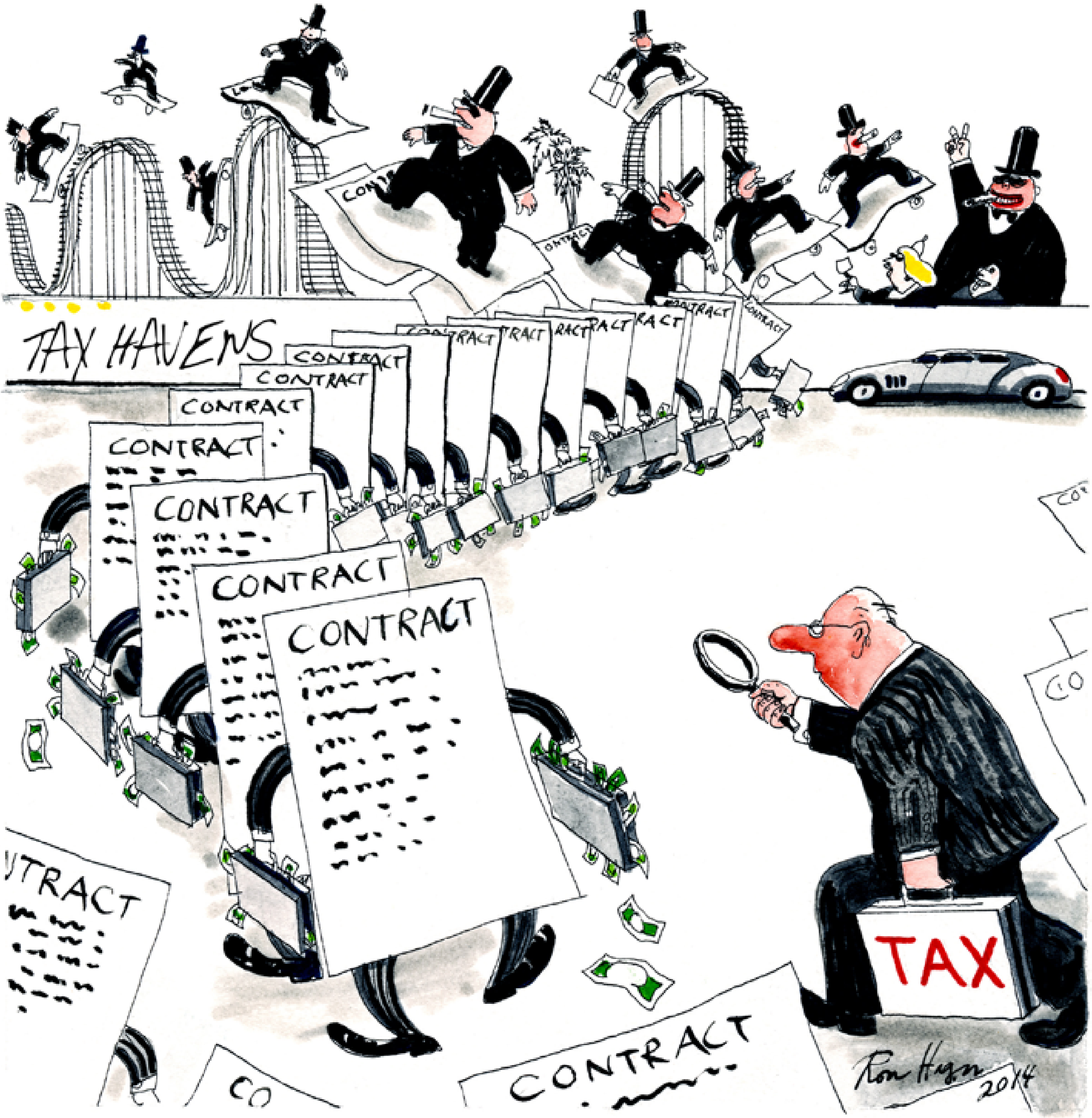
- Tax administrations do not have access to the entire document trail within multinational companies today
- The Transparency Agreement can change this, on a sampling basis, so that tax administrations obtain the insight they need
- The Transparency Agreement can be used by individual countries, or by groups of countries unilaterally

Written by: Frian Aarsnes. Co-Authors; Morten Eriksen and Olav Lundstøl.

Transparency Agreement

– A tool for multinational transactions

How to expand and fix the toolbox of tax administrations



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Transparency Agreement – A tool for multinational transactions

How to expand and fix the toolbox of tax administrations

A recurring problem in the global market is a number of asymmetries between the transnational companies (TNC) and the host countries where wealth is created. And while they are found especially in the developing countries, they are also found in rich countries. These asymmetries stem from the information gap between governments and companies relating to all kinds of natural resources, extractive industry expertise, access to information, etc.

More than 50% of the 100 largest economies in the world today are TNCs, and less than 50% are countries, measured in annual turnover vs GDP. This means that three-fourths of the countries in the world are smaller than these companies. Many of them are extractive companies with operations in countries all over the world; routinely organized through a huge number of subsidiaries in tax haven jurisdictions, and is an unknown number of related party transactions. Not unexpectedly, the companies are growing faster than most of the countries. What is going on in these companies are more or less impossible to unveil for any country, rich or poor. The need for more transparency is obvious.

This report has been written in order to give a complete overview of the transparency initiatives in the world today and to increase knowledge on a lesser known transparency instrument – the Transparency Agreement (or Transparency Guarantee, if demanded unilaterally by a country). The Extractive Industries Transparency Initiative was effectively created at a conference in London in June 2003, during which a Statement of 12 Principles to increase transparency of payments and revenues in the extractive sector was agreed upon. The initiative was a compromise at the time, due to pressure from amongst other major civil society organizations for companies to publish what they paid in taxes. It focused on a voluntary process involving authorities, companies and civil society. At the time of this report there are 25 EITI-compliant countries, and 16 EITI candidate countries.

EITI reports are limited to single country information and do not cater to the need for an all-encompassing reporting process in which each company reports on all the countries in which they are present. From the experience between BP and Angola, which is part of the EITI history, it has become obvious that requiring each company to publish what they pay in taxes is something that needs to be anchored in law. Civil society organizations are pushing for passing laws that ensure that all companies will be required to publish their taxes and related information per country, for all countries without exception (country-by-country reporting or CBC reporting), and such laws have been partly passed in the US and the EU, and more fully in Norway. These laws are currently too weak, as the taxes are not published in their natural context and not as part of the financial statement. Thus, Publish What You Pay Norway has introduced a report titled "An extended country-by-country reporting standard – a policy proposal to the EU".

While EITI takes care of the industry-to-government perspective, and the extended CBC reporting takes care of the company-to-the-wider-world perspective, we are left with the area of company-to-government perspective. This is very much regulated by each individual government, and the government institutions that want insight into the companies usually find that the information they are receiving is limited to the company that operates within their own country. If they want insight into the audit trail of documents all the way through a multinational company until a product is sold to the external market or a cost enters the group, then they are limited to slow and painstaking processes that limit the abilities of government institutions to fulfill their purpose: regulatory framework, oversight, monitoring, and control.

One initiative that has been introduced by government officials in Norway offers potential help, and Publish What You Pay Norway publishes, by means of this report, an investigation on whether or not this initiative could be helpful for resource-rich countries, and in that case, which countries could benefit from it. This initiative is the Transparency Agreement or Transparency Guarantee which has been rising from mere whispers in 2010/2011 until it became a part of a government white paper - Parliamentary report no. 25 (2012/2013) - that was released in April 2013.

The Transparency Agreement is, simply stated, a unilateral contractual arrangement between a company and a government whereby the company guarantees that in exchange for its "license to operate" within a country, it will allow a tax authority or other controlling institutions unrestricted access, on a sampling basis, to the entire audit trail of documents from the moment a cost enters the group until it arrives and is claimed as a deduction in a country, or from the moment a revenue item originates in a country until it exits the group at market prices. For the sampled transactions, it is irrelevant where in the group the documentation exists: all relevant documents are to be provided to the requesting authorities without undue delay. The sampling method and number of sample transactions per year, per category is agreed upon in advance during the initial contractual arrangement in order to protect the company against unnecessarily burdensome documentation. All transactions can be sampled (completeness), but only a few transactions are actually sampled every year (relevance). The Transparency Agreement does not put any restrictions on the access to the national company's records and documents. It is purely an instrument that pre-arranges for access to examples of how transactions flow between the company and external or internal providers (cost) or external and internal off-takers (revenues).

A Transparency Guarantee is the terminology used when a state unilaterally demands transparency in return for a license to operate within the country. A Transparency Agreement is the equivalent form in countries where transparency is part of a negotiated agreement. The content is the same; a guarantee to provide all necessary audit trail documents related to a set of transactions, selected on a sampling basis, by a government institution in the country in question. Through the rest of this report we will use the term Transparency Agreement unless we are specifically meaning the unilateral instrument Transparency Guarantee.

Content

Preface

Tax avoidance. Corruption. Capital flight. Organized crime. Interrelated problems. Add international banks, accountancy firms, legal firms, secrecy jurisdictions, and the many service providers. PWYP Norway has for many years, and in several reports, produced knowledge about the various secrecy mechanisms that are available in the toolboxes of multinational extractive companies to draw a veil of opacity over their transactions and activities, in order to hide relevant information from both a home country and a host country. We have shared our findings and reports with governments, journalists, civil society, the EU, the IMF, and the OECD, amongst others.

A high-level panel in the African Union recently launched the report "Track it! Stop it! Get it!". The report finding is that the continent is losing over $50 billion in revenues every year, money that should have been invested in sustainable development. That means that the continent has lost at least an estimated $500 billion to illicit foreign flows over the past decade.

The high level panel, chaired by former South African president Thabo Mbeki, was set up as part of ongoing AU efforts to reduce the continent's dependence on official development assistance. The continent needs to use to all possible measures to ensure they can finance and respect the development priorities they have set.

The panel found that large corporations account for 65% of all illicit financial flows out of Africa. The mechanisms used are mispricing, incorrect invoicing, shell companies, tax breaks and poor cost-benefit analyses. In his foreword to the report, Mr. Mbeki points out that large corporations have all the resources available to them to retain the best available professional legal, accountancy, banking and other expertise to help them perpetuate their aggressive and illegal activities. The findings compliment IMF findings which pointed out that companies often reallocate income rather than pay taxes, and that developing countries may lose up to 15% in tax revenues. The OECD also addressed tax-planning strategies that exploit gaps in the architecture of the international tax system to artificially shift profits to places where there is little or no economic activity or taxation.

The question then is: which possibilities and mechanisms do a country have, to gain access to vital information?

Publish What You Pay Norway's main focus is to work to ensure that extended country-by-country reporting is legislated in as many countries as possible, to enhance the public oversight of extractive industry companies by investors, governments, media and civil society. The extended country-by-country reporting is a simple, low cost and effective tool that can make the use of the secrecy mechanisms in secrecy jurisdictions irrelevant, when the home country demands information on income, cost, profit and taxes. It is then possible to know in which jurisdiction the financial capital has been accumulated. However, the extended country by country reports cannot address other secrecy mechanisms, such as companies claiming client confidentiality to protect themselves against government insight into activities and transactions, transaction routes and company structures, or how they happened.

Because governments have not yet made use of such simple and inexpensive mechanisms which can provide public oversight, a country will usually look for an instrument that can be enacted unilaterally, and in a timeframe that is acceptable. Previously we have furnished such a mechanism when we promoted a method for protection against abuse of derivatives that any country could introduce unilaterally, independent of any other countries.

But, despite there being a global momentum and call to address these issues right now, there is simultaneously a massive inertia amongst all of the initiatives taken around the world in global institutions to demand information from companies, and to furnish tax administrations and other controlling institutions with the instruments they need to control multinational companies. It takes years, or even decades, from the moment an initiative is launched until it has found its final form internationally, and alas, decades again before one country might actually find out whether or not it works.

We will argue that the Transparency Guarantee or Transparency Agreement that is investigated in this report is another such simple and inexpensive solution that can be introduced unilaterally (as a guarantee) or agreed between negotiating parties (as an agreement). The idea is not ours as such, but our investigation of the idea tells us that the idea is interesting to investigate further. In particular, we believe that resource-rich countries might consider this mechanism as part of a system to pre-qualify companies that want a "license to operate" within a country. If a company declines to agree on being transparent on their transactions, is that truly a company that one would like within one's borders? We wouldn't' think so. And that is exactly the case: the citizens of the country, through their government, collectively own the resources within their country. Citizens also may ask whether or not a government is willing to demand transparency from a company, and if a country is not willing to demand transparency in return for giving away its resources, most citizens will question why that is.

The extractive companies do not own the resources. They are custodians that the country's government entrusts to explore for, develop and market the country's resources. They do not own the profit before that profit has been correctly taxed. Only after-tax profits should flow back to the larger group, for the benefit of being able to pay dividends to the investors that put up the money in the first place. If non-taxed money leaves a country, it has a tendency to end up in tax havens where it cannot be accessed by tax administrations, investors and capital markets. Some companies have so much capital stashed away in tax havens that they effectively form their own banks whereby they finance new investments in resource-rich countries using money that has been withheld from public control, whether it be by investors, financial markets or governments. The same companies have to borrow money to pay dividends to their investors, because their cash flow is locked within tax havens and tax payments will be triggered if the money is used to pay those who furnished the capital. This is a flawed system, and it actually undermines governments, financial markets and investors alike, as well as endanger the very societies in which we live, because it leads to social unrest, political strife, conflict and in the worst cases violence and (civil) wars.

In many reports we have argued for simple and cost effective solutions and mechanisms that may address the massive problem of capital flight and corruption that we see in the world, and which is particularly present in resource-rich countries, in non-renewable industries and renewable industries. This is one of those solutions, which is available for countries' own tax administrations.

It's time for resource-rich countries' tax administrations to also have a toolbox available to them to handle the massive problem of capital flight and corruption.

Our suggestion, then, is that you take the time to read this report, particularly if you are a government official, a journalist or a civil society representative in your country, and decide for yourself whether the concept that has been investigated in this report is something that could be useful in your country. And then perhaps you could discuss the idea further with others?

Mona Thowsen
Secretary General
PWYP Norway

If the reader would like to share any comments, viewpoints or information, or has any questions or suggestions for further investigation, please contact us at: post@pwyp.no.

1. What is a Transparency Agreement?

A contract-based Transparency Guarantee can loosely be described as an agreement with a company to not use secrecy mechanisms to hide relevant information from a host country in return for access to a country's non-renewable and finite resources. The basis for the Transparency Guarantee is that a company is the custodian upon whom countries rely to ensure that products will be extracted and marketed to the benefit of both.

A major problem is that governments in host countries have no or very little access to vital information that could ensure a fair profit-sharing between the host countries and the extractive companies. It is not acceptable that, instead of open books from the companies to the host countries, these countries have to face extremely expensive and time consuming court hearings in several tax haven jurisdictions to gain access to information. In practice this is not a realistic way to gain access to information needed.

The G 20-countries have called for more efficient initiatives to ensure that multinational enterprises will avoid artificially shifting profits to low-tax jurisdictions. In a statement endorsed by the G 20-countries, the following was stated, among other things:

> *"Profits should be taxed where economic activities deriving the profits are performed and where value is created. In order to minimize BEPS, we call on member countries to examine how our own domestic laws contribute to BEPS and to ensure that international and our own tax rules do not allow or encourage multinational enterprises to reduce overall taxes paid by artificially shifting profits to low-tax jurisdictions."*[1]

The Transparency Agreement described in this report fits well into the invitation from the G 20-countries.

It is a firmly established concept in most countries that ownership to any natural resources in the ground or below the seafloor rests with the citizens of a country through the state, and that any revenues from these resources are to be taxed within the country.[2] It is the state, through the relevant institutions, that ultimately gives a company the right to explore for, develop and produce such non-renewable natural resources. This right is often termed "license to operate" and is a concept that prohibits a company from carrying out an extraction-related business without the required formal approvals. This is in contrast to other industries, in which the government's role in most cases is to ensure that anyone can start a business in fair competition with any others in the same type of business, or to secure that there aren't any market failures (over-capacity, under-capacity, monopolistic pricing or other forms of mispricing).

The fact that a state gives the right to explore, develop and produce non-renewable resources to individual companies means that the state can also set the conditions that the companies must operate under. These conditions are typically of technical and operational, external and internal environmental, fiscal or social nature. Some conditions are so fundamental that it is a precondition that a company fulfill certain requirements in order to seek business in the country. Being transparent towards the country that has *given* the company the right to explore, develop and produce must be an item so fundamental that it becomes a part of the preconditions a company must fulfill in order to do business in the country, i.e. it must be one of the conditions a company must agree to in order to receive its "license to operate". The reason why this is fundamental is that when a company or several companies are given the right to explore in an area, one is effectively giving a monopolistic license to the company/companies in question. And in almost all countries it is the same company/companies that are given the right to develop and produce any resources discovered, although the best companies to explore are not necessarily the same companies that are best at developing the resources.

1 Addressing Base Erosion and Profit Shifting, Tackling Tax Avoidance, and Promoting Tax Transparency and Automatic Exchange of Information, section 50

2 Even in countries like the US, where private citizens own any natural resources below their land, there are public institutions that will have to approve before development of a resource. The US is, however, also a country that adheres to the principle that any profits from extraction of natural resources inside the US borders are to be taxed within the US borders.

A country needs to pay particular attention to industries in which there are monopolistic tendencies or characteristics. Once an area is licensed to a company/companies, it is to the exclusion of all other companies. Thus it does not help that other companies are able to get other licenses in other places. The monopolistic characteristics are still there because the right to explore, develop and produce is to the exclusion of everyone else. The Free Dictionary defines monopoly in 4 different ways, and the right *given* to extractive companies fulfills all four definitions:

- *"Exclusive control by one group of the means of* ***producing*** *or selling a commodity or service".*
- It is very clear that we are talking about exclusive control of production of a commodity.
- *"A right granted by a government giving* ***exclusive control*** *over a specified commercial activity* ***to a single party****".*
- *It is very clear that a government has granted exclusive control over the license (hence the term "license to operate") to a single party, although the party can consist of a group of companies that share the same interests.*
- *"A company or group having exclusive control over a commercial activity or a commodity or service so controlled".*
- *It is very clear that it is a non-renewable service that is being produced, and that the extractive company thus is a custodian providing a service to the country.*
- *"Exclusive* ***possession*** *or control"*
- It is very clear that the extractive company has exclusive possession and control over the products throughout the entire process until they are sold in a market place.

What we are talking about is not that there are monopolistic characteristics in the market where the products are sold, only that there are monopolistic characteristics in the ways in which extractive companies are given rights to valuable areas to the exclusion of others. This has important implications regarding the transparency needed; amongst others, to ensure that there is competition between companies when licenses are awarded in order to avoid collusion or the suspicion of collusion between companies and government officials when a license is granted.

A Transparency Agreement should thus be entered into with the company, in exchange for the "license to operate" that the government gives to the company in order to overcome (1) the exclusive possession and control that the company has over the resources given while exploring, developing producing and selling them, and (2) the information gap that exists between the company and the government as a result of that exclusive possession and control.

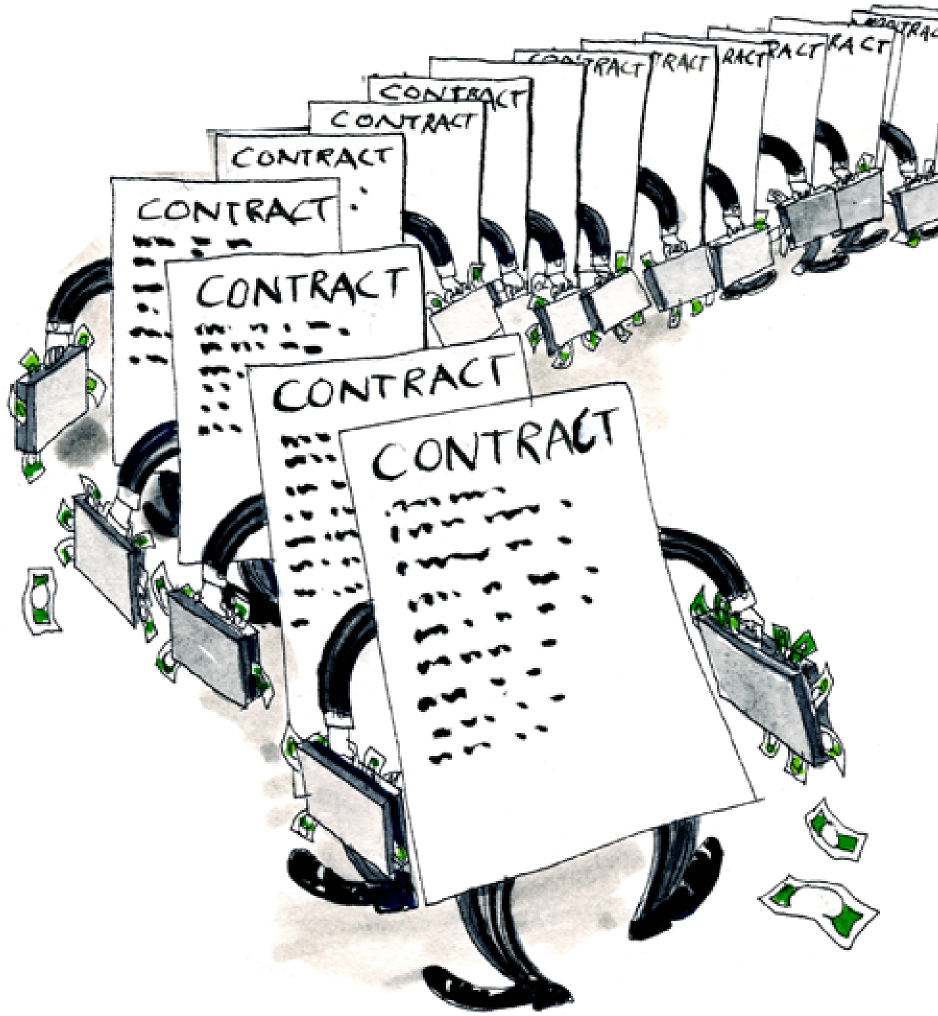
We can now define this particular transparency initiative in more detail:

Transparency Agreement	Transparency Guarantee
The Transparency Agreement is a negotiated contractual arrangement *between a company and a government* whereby the company guarantees, *in exchange for its "license to operate" within a country, that it will allow a tax authority or other controlling institutions unrestricted access, on a sampling basis, to the entire audit trail of documents from the moment a cost enters the group until it arrives and is claimed as a deduction in a country, or from the moment a revenue item originates in a country until it exits the group at market prices.* *For the sampled transactions, it is irrelevant where in the group the documentation exists: all relevant documents are to be provided to the requesting authorities without undue delay.*	*The Transparency Guarantee is a* unilaterally introduced arrangement *between a company and a government* whereby the company is obliged to guarantee, *in exchange for its "license to operate" within a country, that it will allow a tax authority or other controlling institutions unrestricted access, on a sampling basis, to the entire audit trail of documents from the moment a cost enters the group until it arrives and is claimed as a deduction in a country, or from the moment a revenue item originates in a country until it exits the group at market prices.* *For the sampled transactions, it is irrelevant where in the group the documentation exists: all relevant documents are to be provided to the requesting authorities without undue delay.*
The sampling method and number of sample transactions per year per category is agreed ahead in the initial contractual arrangement *in order to protect the company against unnecessarily burdensome documentation.* *All transactions can be sampled (completeness), but only a few transactions are actually sampled every year (relevance).* *The Transparency Agreement does not put any restrictions on the access to the national company's records. It is purely an instrument that pre-arranges for access to examples of how transactions flow between the company and external or internal providers (cost), or external and internal off-takers (revenues) outside of the country in question.*	*The sampling method and number of sample transactions per year per category is agreed ahead in the* initial unilateral arrangement *in order to protect the company against unnecessarily burdensome documentation.* *All transactions can be sampled (completeness), but only a few transactions are actually sampled every year (relevance).* *The Transparency Guarantee does not put any restrictions on the access to the national company's records. It is purely an instrument that pre-arranges for access to examples of how transactions flow between the company and external or internal providers (cost) or external and internal off-takers (revenues)*

A Transparency Agreement is something all countries can utilize as it is a negotiated instrument.

A Transparency Guarantee is not something all countries can readily introduce as it is a unilateral instrument. Before the Transparency Guarantee becomes an accepted instrument among many countries it is mainly countries with high prospectivity that can consider this instrument on a unilateral basis. However, larger or smaller groups of countries can introduce it unilaterally for an entire region or for a particular type of commodity. Examples of larger groups of countries introducing it could be countries in the African Union, while examples of smaller groups of countries introducing it could be countries within SADC or Former Soviet Union republics, countries that are major producers of a specific commodity, for example copper-producing, gold-producing or oil-producing countries like Norway, etc.

The important thing is that the Transparency Agreement and the Transparency Guarantee are instruments that are available to interested countries, should the need arise. A history of abuse of previous contracts by extractive companies, a history of companies which do not have profitable production even at high prices, and a history of a tax administration that does not have the competence, the capacity or the funding to follow up on extractive companies, are examples of situations that warrant the use of an instrument such as the Transparency Agreement or the Transparency Guarantee. And yes, the intention is to get rid of the abusive companies and remain with the companies that are willing to share at the table.



2. The Transparency Guarantee in White Paper No. 25 (2012-2013)

The following is a full, yet unauthorized, translation of the Norwegian White Paper describing a Transparency Guarantee as it has been published by the previous government in Norway (2009-2013):

> *"The (Norwegian) Government will promote the initiative of developing a Transparency Guarantee for use by governments in developing countries. The guarantee ought to secure these governments adequate access to information from extractive companies. The Transparency Guarantee will be promoted through relevant development programs.*
>
> *Confidentiality and tax havens are used to limit access by authorities to documents. The purpose of a Transparency Guarantee is that it secures that documents that are relevant for the developing country's government become accessible as case documents, and that a potential dispute is about the interpretation of the documentation, not about the obtaining (of the documents).*
>
> *A Transparency Guarantee ought to secure that the authorities gain access to documents from companies abroad in connection with transactions that cover several companies in the same group. It ought to contribute to transparency and understanding between the individual extractive company and the authorities the company reports to, mainly the tax authorities, but not limited to these.*
>
> *The tax authorities' access stops today when transactions relate to a company's activity outside the country. In the development of a Transparency Guarantee the aim is that the tax authorities gain access to relevant documentation in a transaction chain within the company group, a so-called audit trail. When for example minerals are sold, it means that the tax authorities on request can follow the sale from production country through affiliated companies in several countries, including tax havens, and all the way to the first buyer outside of the company group.*
>
> *Key questions in the development of a Transparency Guarantee is amongst other how far the companies' information duty goes and how far the risk of sanctions go. A Transparency Guarantee ought to secure that it is possible to track a product all the way until it is sold in the open market. The tax authorities will then have a basis for assessing whether the revenue that the company has included in their tax return is correct. The same will apply for the transaction chain for a deductible cost.*

> *Violation of the Transparency Guarantee should lead to sanctions if the company has access to the requested information. Sanctions must be proportionate, and could be tested legally. In extreme cases a possible breach of the Transparency Guarantee could include revocation of the extraction license (the license to operate). But sanctions need to be proportionate, predictable and verifiable for the companies.*
>
> *A Transparency Guarantee should apply equally for all companies. It is up to the individual country to evaluate whether they want to implement this through a model agreement or through law. The purpose of the Transparency Guarantee falls away if it is made into a negotiable position between the authorities and the individual company, resulting in different demands for transparency from different companies.*
>
> *In many developing countries the companies with the worst standards of transparency have a competitive edge. The goal for the development of a Transparency Guarantee is that this should contribute the companies having to comply with the same standard and provide a more equitable competition, better tender processes and less room for corruption.*

The intention of the Transparency Guarantee is to ensure more level competition for the benefit of companies who behave responsibly, and to the detriment of companies who want to dodge their responsibility to contribute to the society from which they have received their revenues. Their contribution should be to explore for, develop and produce the resources at the minimum cost to the host country, and to sell their production for the highest prices in the market place or, if sold internally for further processing, that it be sold at the same prices as it could have been sold at to other processers. Many companies will tell politicians that they are constantly working to maximize revenues and minimize costs. This is true, but only seen from the group level. When one goes down to the individual company level in host countries, there is a massive reduction of revenues and a massive increase of costs at the expense of the host country, and to the benefit of tax havens.

Transparency Agreement

3. What is the purpose of a Transparency Agreement/Guarantee?

The purposes of the Transparency Agreement is crystal clear: *"that the companies will have to comply with the same standard, and provide more equitable competition, better tender processes and less room for corruption"*. It cannot be said more purposefully.

Any kinds of disputes concerning access to vital information between a transnational company and the host-country must be solved in the court – unless they come to an agreement. After a conflict has arisen, the likelihood of an agreement is very slim, hence the need for establishing such an agreement beforehand. Access to information via court hearings is extremely expensive and time consuming. The chances of gaining access to substantial information are rather limited. From any realistic perspective, the court system works in favor of the companies. It is an overwhelming documentation that shows the negative consequences of lack of access to information for host countries.

There are strong reasons to believe that the asymmetries – in all respects – between the host countries and the companies will increase in the future. Of the 100 biggest economies in the world today, more than 50% are transnational companies. This means that these companies are bigger (annual return) than the gross national products of three-fourths of the countries in the world. And the companies are growing faster than the countries. Whilst the countries basically operate within strict limited borders, a transnational company operates worldwide as one economic entity.

Thus the Transparency Agreement aims at compensating the imbalance in relative strength between the companies and the host countries. It can be a very useful alternative vehicle to court cases, and necessary information to give the host countries a fair share of value created in the extractive industry.

The purpuse of and benefits from transparency can be summarized in 10 points:

1 It will reduce the negative impacts secrecy has on fighting poverty in developing countries.

2 It will strengthen resource-rich developing countries' positions in negotiations with TNCs. Either a sustainable Transparency Agreement, or no license to extract natural resources.

3 It will reduce the risk of corruption, manipulated transfer pricing, misgovernment, mismanagement, tax fraud, and illegal trade of various kinds.

4 It will make governments responsible to their citizens. Transparency clauses in existing and new contracts will be comparable to model agreements or legislation that impose Transparency Guarantees.

5 Reluctance to enter into a Transparency Agreement will be self-exposing both to the companies and corrupt governments.

6 It will hopefully reduce the role of secrecy jurisdictions, and reduce demand and supply of secrecy mechanisms, abuse of legal privilege, etc.

7 It will contribute to avoid endless and extremely time-consuming letters of request, and court cases in several jurisdictions, just to gain access to information.

8 It will encourage and reward investors, governments and companies that prefer fair competition in transparent markets, rather than secrecy and competition in concealed markets, and corrupt behaviour.

9 It will send a strong signal and encourage countries with poor transparency record to operate transparently.

10 It will give developing countries better ability to control their most valuable resources to achieve economic growth. It makes it possible to test and investigate, in advance, the willingness of the companies to comply with the various elements in a Transparency Agreement.

Transparency Agreements are by far the best, most efficient, most easily introduced and quickest available response to the harmful secrecies in the global market in the world today.

The situation today is that the worst companies are leading a negative race to the bottom; the bottom of economic benefits from natural resources, the bottom of the fight against corruption, the bottom of competition and, in essence, to the bottom of morals and civilized society. The Transparency Guarantee flips the picture: the worst companies will have to live with the standards the best companies can thrive with. The goal is to give preference to companies that are best at competing in a transparent environment, and thus contribute to avoiding corruption and what was described as "artificially shifting profits to low-tax jurisdictions" in the G 20-meeting in St. Petersburg last year.

It is the purpose to create a standard that the best companies can thrive with. Thus a Transparency Agreement cannot be an instrument under which a company takes on an ultimate responsibility to deliver everything requested from a tax authority or other controlling institutions. There must be limitations with regards to the number of transactions that a company will have to provide full documentation on, in each category per year. The purpose is not to take out the good guys; the bad guys are the target.

Essentially, the purpose is to create a mechanism that exposes the worst companies maximally, and creates the least amount of burden for the best companies. The purpose is to create change within the worst companies, stopping the downward spiral among the best companies.

A contract-based Transparency Agreement can address the paradox of today's situation in which an extractive company is able to gain access to non-renewable and finite resources without having to be transparent towards a host country's authorities when they ask for relevant documentation on the company's structure. A contract-based Transparency Agreement will demand that companies do not use secrecy mechanisms in order to hinder such insight into documents located in other companies within the company. This is particularly important for developing countries as they may often be at a disadvantage, both in terms of information (information asymmetry), and in relation to capacity (legal capacity asymmetry). However, in order for such an instrument to function optimally, it is necessary and crucial to focus on what is the correct use of such an instrument, what is the right level of use and what constitutes the right user group for such an instrument.

We will come back to that in chapter 8 when we analyze the benefits and the threats of a Transparency Guarantee.

4. Why is a Transparency Agreement important for PWYP Norway?

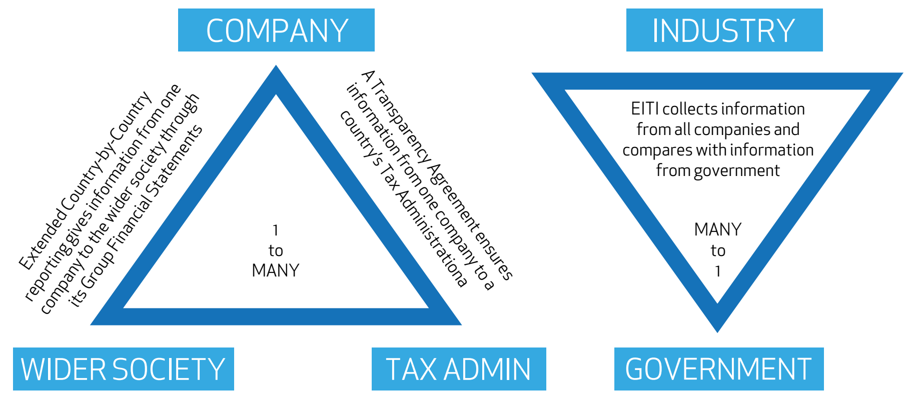
The idea of a Transparency Guarantee is not with PWYP Norway. The idea came from a government official in Norway and ended up as part of a potential foreign policy change in the 2013 government white paper. PWYP Norway does not promote the Transparency Guarantee itself, but we wanted to investigate how a Transparency Agreement or a Transparency Guarantee initiative fitted into the bigger picture of transparency in extractive industries, and it sure has a purpose in the bigger picture.

PWYP Norway's goal is the introduction of extended country-by-country reporting into law, to ensure that every extractive company has to produce the same standardized data on taxes in their natural context, for every country in which they are present, without exceptions. This is actually for the protection of the companies, so that no company voluntarily releases information while other companies do not. We are concerned with ensuring fair competition among the companies in order to promote the best companies.

PWYP Norway has promoted transparency ever since it first formulated and promoted the establishment of the Extractive Industries Transparency Initiative (EITI). EITI has now become an instrument for those countries that want to show that there is a match between what governments claim are paid, taxes, and what the companies claim they pay. EITI was a first step in transparency, but EITI in itself is not the goal. The goal is to have every extractive company become transparent about their business in every country in which they are present, no exceptions, in return for their license to operate.

There are limitations to what EITI is capable of. EITI cannot take on the individual company's responsibility to be transparent. The next step after EITI is thus for the individual company to be transparent, and this has to be at two levels:

- the company has to be transparent towards its investors and the broader society when it comes to activities in a country and the countries where revenues or costs arise internally
  --> is solved by extended country-by-country reporting
- the company has to be transparent towards the tax authorities in a country as the custodian of the extraction of natural resources in the country
  --> is solved by Transparency Agreements or Transparency Guarantee



PWYP Norway has previously published the report "An extended country-by-country reporting standard" in order to show that it is actually easy and cheap to publish transparent information in, and in conjunction with, the company's consolidated financial statements towards the wider society. This reporting will take care of the transparency needs towards investors and society at large, but it will not be capable of satisfying the needs of tax authorities (as EITI is not capable of either – see figure above).

Extended CBC reporting secures the transparency between the company and its investors and the wider circle of constituents. There is a hole in the transparency net, though, and that is how a country can protect itself against the worst companies, i.e. how to create true transparency between the individual company and a government. For this one needs an instrument that can demote the worst companies without hurting the good companies. After having analyzed the Transparency Agreement and the Transparency Guarantee, we are convinced that these are the instruments countries need in order to keep the worst companies away from positions in which they are able to pay minimal or no taxes, and in which corruption can be promoted, with monopolistic characteristics. However, the intention is not to keep them out at any cost. The intention is, rather, to force them to change their destructive behavior and report at the same level as the best companies.

When it comes to the implementation of a Transparency Agreement in a country, it must be the government and the tax administration in the country in question, backed by civil society, to decide whether the Transparency Agreement is viewed as a good instrument in that country. The reason for this is that while EITI is a worldwide initiative pushed by civil society and governments in many countries, and the extended country-by-country reporting is a universal mechanism for how to create a uniform reporting standard for multinational companies, the Transparency Agreement is a mechanism which needs to be tailored to, and implemented in, each individual country. PWYP Norway's role is to investigate the circumstances under which a Transparency Agreement or a Transparency Guarantee can work, and create an operational platform on which such an initiative can be built in a country. PWYP Norway's role has been to put together this report in order to clearly describe the mechanism and analyze the benefits and the threats associated with the mechanism.

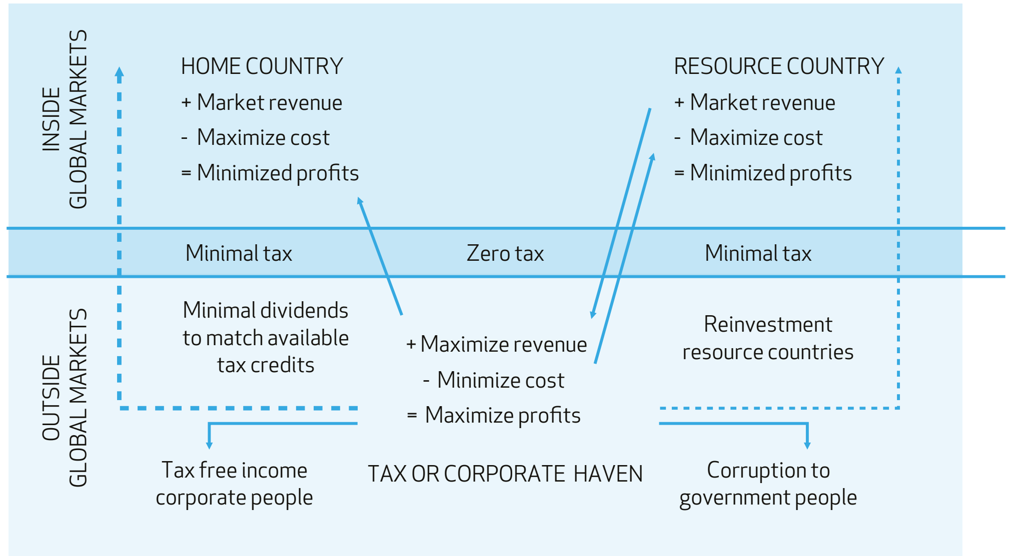
5. How can we understand a Transparency Agreement in the broader framework of a country's tax regime and tools?

What most people do not understand is how difficult it is for a tax authority to assess a company that belongs to a group that purposefully moves pre-tax profits out of a host country through mechanisms that reduce the revenues or increase the costs within the country.[3] The only information that a tax authority, or another controlling institution, is able to access usually involves documents that pertain to the company within the country, and usually no information is available for the full audit trail all the way to or from an independent third party outside of the group.

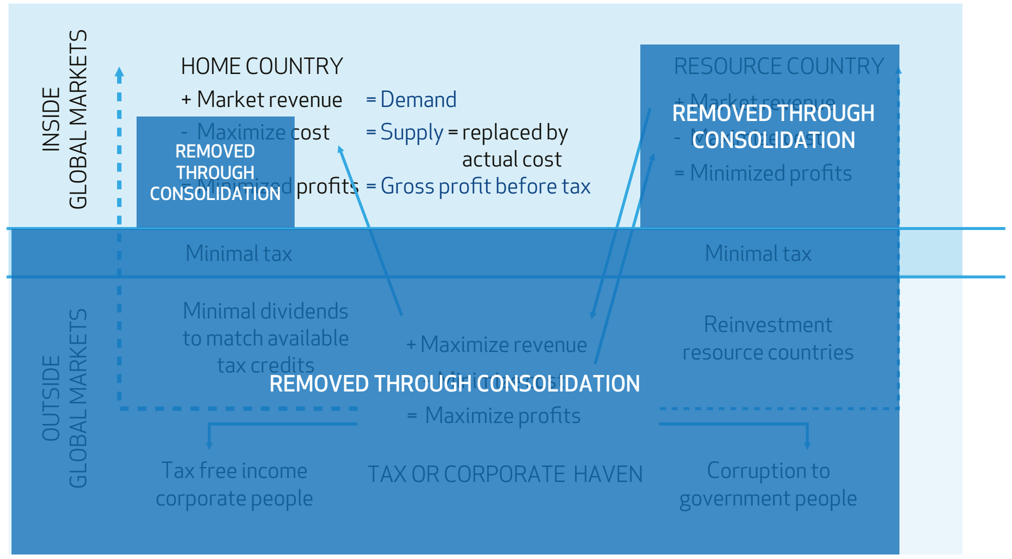
The following is just a sample of obstacles to an effective assessment of a multinational company's tax return in a host country:

- the tax administration usually only has access to those parts of a transaction chain that are internal within the country or which cross the national border. It is not possible to follow the audit trail of documentation until a product exits the group or until a product or a service enters the group.
- the tax regimes in most countries are not set up to tax multinational companies, only national companies. The tax regulations, therefore, treat multinational companies as if they were national companies, and indeed, they are not.
- the transfer pricing guidelines issued by the OECD only compound the problem as, for the most part, they massively promote the arm's length principle as the sole remedy for treating intra-group transactions. This means that transactions within the group are treated as if they were made externally. Even in countries with quite sophisticated tax regulations, we have seen that companies are able to transfer massive amounts of pre-tax profits to tax havens through inconspicuous charges for "services" done out of these tax havens. However, there is almost no substance to these charges as there is no cost base to take them against, or the cost base is in another country which does not receive the revenue which effectively is captured in between by the tax havens. There are four major reasons why transfer pricing regulations are too difficult to succeed: 1) The regulations are far too complicated to maintain, with many disputable exercises in discretion, 2) It is far too difficult for the governments to gain access to relevant information, 3) There are significant asymmetries between the company and the governments with regard to the expertise needed to evaluate the pricing, and 4) Disputes will easily end in the courts, and favor the companies that control the facts.
- there are several options for the companies to invoice various costs from tax havens, in spite of little or no value creation having taken place in the tax havens. However, due to lack of information this is very difficult to control.
- to compound the problem, most tax administrations are focusing their efforts on companies that make profits, and tend to not follow up so much on the companies that show no profits or negative profits, although the group financial statements show that the companies are making massive amounts of profit.

3 See www.pwyp.no for reports documenting this, including a report on derivatives abuse, a type of pre-tax profit shifting that is almost impossible for the tax authority to uncover. However, there are valid ways to ensure that such abuse cannot take place, but they require changes to tax laws in the countries in question.



The major problem is that governments, creditors, investors etc., can be shown a very limited and misleading picture:



Nobody sees the whole picture from the outside, and actually very few inside a company see the whole picture. The figures illustrate how home countries, where one finds most extractive industry companies, are mainly losing their tax base through mechanisms that increase the costs within home country companies. Products are usually sold into the market at market prices, as the tax administrations in these countries are usually pretty good at assessing the revenue side of these companies (but even there one sees massive losses of revenue from time to time). The graphs also illustrate how host countries, where one finds most of the natural resources, are losing their tax base through mechanisms

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The barriers do not stop there, though. In 2007 Norway took an international initiative together with interested countries and voluntary organizations to create a forum that developed into the Task Force on Financial Integrity and Economic Development. This group is headed by leading civil society actors and academics, and the opinions do not necessarily coincide with the member states' views. Countries that are associated with the initiative give their general support to financial transparency and integrity for the benefit of economic development in general and for developing countries in particular. The five main goals are:

1) Country-by-country reporting for multinational companies (however, to date Norway has failed to introduce effective country-by-country regulation which puts tax payments in their natural context, provides key financial numbers, and which puts the reporting in notes to the financial statements for all countries, no exceptions).

2) Automatic exchange of tax-related information (however, Norway has failed to realize that this is a very good initiative for static fortunes stashed away in a tax haven, but a very bad initiative for following the cash flows of a multinational company as it moves in and out of tax havens and other jurisdictions --> the only mechanism is the extended country-by-country reporting standard as identified under 1 above, backed with efficient Transparency Agreements).

3) Limiting the transfer mispricing on trade (however, Norway has failed to introduce the only mechanism that truly uncovers the results of transfer mispricing as per the graph above --> the extended country-by-country reporting standard as identified under point 1 above).

4) Transparency about licensees and beneficial ownership.

5) International harmonization of white-washing laws.

It is important to underline the need for countermeasures that are effective without consent from, or need to change the laws in, secrecy jurisdictions. Transparency Agreements are the only available vehicle that give the host countries power to affect the relative strength of transnational companies, as they control to whom, and under which conditions, licenses are given.

When even countries like Norway, which started the initiative, are not able to fully implement an instrument such as extended country-by-country reporting, which addresses all the three first points on the list, one should not be amazed that other countries are not able to pull their tax regulations together and challenge the multinational companies that are utilizing the tax havens to accumulate pre-tax profits for their own benefit at the cost of host and home countries. It has been demonstrated again and again that many companies treat the resources as their own once the license to operate has been received, and the companies are not transparent towards the tax authorities in the countries in which they operate. Companies stall, hamper, deny, lie, and downright threaten in order to avoid having to produce the documentation to prove their tax return is in order. This fact is, often only realized after they have received their license to operate, and by then it is often too late. The country is "married to" the company.

The extractive company is, however, the custodian for a country's government in the effort to monetize oil & gas and mineral resources for the benefit of the country. The Transparency Agreement is a mechanism whereby countries, prior to giving the companies licenses to operate, can investigate the companies good will in their role as custodians of natural resources. A Transparency Agreement thus ensures that only the companies that are willing to give the tax authorities insight into audit trails for both revenues and costs, on a statistical sampling basis or selected transactions, through all the internal chain of companies, will obtain a license to operate. Companies will have to provide documentation, without recourse to legal actions, delays or otherwise hindering the tax authorities from obtaining the documentation needed on a timely basis, when such samples are required by the tax authorities.

The Transparency Agreement fits into the picture because, unlike the extended country-by-country reporting standard, it exposes individual transactions to the tax administration. What the Transparency Agreement does is enable the tax administration to follow, for a sample of transactions, the entire audit trail for any revenue or cost transaction through the group structure until the transaction chain meets with an independent third party. Only this way can a tax administration be certain that they are comfortable with the pricing of revenues and costs in the company within the country. EITI was one step in the right direction. Extended country-by-country reporting is another vital step in the right direction. The Transparency Guarantee, for the prospective countries that can utilize it, can be the

6. Which transparency categories do we have?

6.1 Three levels, three types and three forms of transparency

To date we have mainly discussed the three levels of transparency with the corresponding three types of transparency:

- Level 1 Industry vs government --> EITI
- Level 2 Company vs investor & society --> extended country-by-country reporting
- Level 3 Company vs tax authority --> Transparency Agreement or Transparency Guarantee

However, in order to complete the transparency map, we must also discuss the three forms of transparency with regards to the opposite: confidentiality.

There are three forms of transparency covering one to three levels, depending on the form.

- Process transparency: always transparent
- Contract transparency: time-dependent transparency (society) and volume/materiality/relevancy transparency (government)
- Transaction transparency: EITI (voluntary - agreement), extended country-by-country reporting (mandatory - law), Transparency Agreement (voluntary - agreement) or Transparency Guarantee (mandatory – agreement)

The alternative to transparency is opacity. This has demonstrably had serious consequences for the environment, markets, societies and individuals in the past. Opacity is thus clearly not a sustainable alternative to transparency if we want resource-rich societies and the best companies to thrive. Transparency is, therefore, the only sustainable alternative. However, transparency is a multi-faceted tool, and we must finalize the discussion on transparency before we analyze the benefits and threats of introducing the Transparency Agreement in a country.

The various forms of transparency can be summarized this way when mapped against levels and types:

	Confidentiality	Process Transparency	Contract Transparency	Transaction Transparency
LEVEL 1: Industry vs government	N/A	Always transparent	N/A	EITI
LEVEL 2: Company vs investor and society	Negotiation phase	No	When negotiation phase is finished	Extended country-by-country reporting
LEVEL 3: Company vs tax authority	N/A	No	Transparency Agreement / Guarantee	Transparency Agreement / Guarantee

6.2 Confidentiality: Negotiation phase

There is one phase in which confidentiality must be respected, and that is during the early stages, when a company is preparing to enter the country or enter into a transaction. During the negotiation phase the company is vulnerable to having its details revealed to competitors, and confidentiality must thus be the general rule as long as negotiations are ongoing.

The consequence of confidentiality during negotiations, though, is that the authorities must always have clear and transparent regulation around the processes involving the industry. We will come back to that in 6.3 below.

For a company that has nothing to fear with regards to the contract it entered into, the need for confidentiality stops when an agreement has been reached, or soon thereafter. There is an intermediate phase particularly when entering a new country during which, for commercial purposes, a company might want to keep a low profile in order to secure personnel for management positions etc., before going public. One has seen no detectable consequences of going public immediately once licenses have been awarded in countries which have transparent processes; a fact that essentially undermines the argument that it is necessary to keep agreements confidential after the negotiation phase is finished.

The general rule should thus be that confidentiality effectively ends when a contract has been through negotiations and duly signed. Effectively, confidentiality is only relevant at level 2: company vs investors and the society at large. Level 1 is not relevant at the company level and there should be no confidentiality towards the tax authority as that institution is set to oversee that the content of a contract is adhered to. A tax authority necessarily needs insight into what has been agreed, and thus needs transparency of contracts relevant for the period being assessed.

The fact that there is confidentiality while negotiations are ongoing is, however, double-edged. Confidentiality requires stringent regulations on the government side when negotiating in order not to create different business conditions for different companies that are entering at the same time. This is difficult, as many countries have a culture for negotiating the "best" position with each and every party. However, past experience tells us that most countries are not able to negotiate a "best" position due to the information gap between company and government.

What most government negotiation teams fail to realize is that the companies and the government are coming in from different positions when negotiations start. Most government negotiation teams seem to believe that their role is to secure investments for their countries. However, when a company enters a negotiation, it has usually done its homework ahead of the negotiations. The fact that the company is entering the negotiations means that they have, in most cases, already cleared away any obstacles for entering the country, and the company wants to ensure that no other company gets more favorable conditions than itself.

The easiest countries for companies to enter are those in which the conditions for entry are regulated and clearly communicated, without any exceptions. It is actually more difficult to enter countries where they have to negotiate, because then the companies will have to negotiate as much as possible in order not to begin in a worse position than their competitors. This stems from the fact that, in many cases, the next company entering a country does not know the conditions offered previous companies because those previous contracts are confidential. Confidentiality thus becomes the enemy both for the government negotiation teams and for new companies entering a country.

Therefore it is not out of ill will for the country that even "good" companies are negotiating fiercely as long as negotiations are allowed. It is in order for them to be in the same competitive position as their competitors.

The second-best thing for a country to do is to secure that all governing contracts are made public when the contract is signed.

The best thing a country can do is do away with negotiations altogether and create common rules that all companies must abide by if they consider entering the country.

6.3 Process transparency: Always transparent

The process between the extractive industry at large and the relevant government should always be transparent. Government documents governing the industry should, as a general rule, be transparent and be presented during hearings to the industry, amongst others. The industry's hearing response should also be transparent.

Without open and transparent processes, a government opens itself up to criticism, media attention, civil society attention and issues involving bad governance, including corruption.

When processes between the industry (not the individual company) and the government are transparent, it is much less probable that the worst companies can influence industry organizations and government officials. The reason for this is that, for example, the industry's hearing documents will be open to the public, including other companies, and it will be quite easy to spot whether invalid arguments have been used towards a government.

Confidentiality around industry processes can only do more harm than good to a country, and thus the best thing that can be done is to make sure that processes are always transparent.

We will underline the importance of process transparency to avoid corruption and manipulated transfer pricing. The tax base must not be "negotiated away" with help from bribes and corrupt behavior.

6.4 Contract transparency: Time-bound and recipient-bound transparency

As concluded in the report "Contracts confidential"[4], *contract transparency is critical to addressing better resource management and bringing contract stability to an industry that sees its contracts renegotiated more than any other.*

A contract need only to be confidential to the wider public in its negotiation phases, or when the contract is at a detailed level, or when the contract is between the company and an employee. Contract transparency normally means that the governing contracts between company and government are made public in order to facilitate a level competition.

After the negotiation phases are over, the contract is supposed to be implemented, and then it is necessary for a number of parties to be aware of the contract. It is thus always highly beneficial to publish major contracts, especially those with environmental, societal and fiscal consequences. This will again ensure that a government does not open itself up to criticism, media attention, civil society attention and issues involving bad governance, including corruption. If a contract is kept confidential, there will always be suspicion regarding the reasons for why it was kept confidential. A government should never accept a company request to keep a contract confidential as it is highly important to ensure level competition amongst companies, and then contract transparency is of the essence. This point is highlighted in the above-mentioned report "Contracts confidential":

> *"Instead, confidentiality clauses, a common and legitimate feature in contracts between private parties, are being used to prevent information from coming into the hands of public groups; while in practice, contract secrecy among private entities is relative. Within the industry, supposedly confidential contracts are bought and sold, analyzed, and even ranked. Some contracts, or essential details of their terms, are disclosed to investors pursuant to securities regulations. Others are shared among colleagues on electronic mailing lists. For larger projects, competitors are often co-parties to the contract, giving them de facto access. This information asymmetry, with companies having much more access to contracts than governments do, may be one reason why companies have not raced to embrace contract transparency. When a company has such an advantage over counterparty, it will logically seek to keep it in order to negotiate a more favorable deal."*

To continue keeping contracts confidential is to continue the information asymmetry between the companies and the governments, and is only in the companies' interest, not in the interest of governments.

Not all contracts are material, though, and transparency of all contracts, material and immaterial, may actually confuse matters. Some contracts are also market-related, and although they may be material, there is stronger weight on the company's argument that these contracts should be kept confidential because they are commercially sensitive. Contracts relating to individual transactions are typically documents that can be transparent between the company and the relevant tax authority, and thus the Transparency Agreement presents itself as an arena for transparency in this area.

One can thus argue that there is time-bound and recipient-bound transparency within contracts:

	Time-bound transparency		
		Recipient-bound transparency	
	Negotiation phase	Contract transparency (public)	Transparency Agreement (tax authorities)
License to operate	Confidential	Always transparent	N/A
Governing contracts with environmental, societal or fiscal consequences	Confidential	Always transparent	N/A
Detailed contracts with environmental and societal consequences	Confidential	Transparent	Transparent
Market contracts with fiscal consequences	Confidential	Confidential	Transparent

4 Peter Rosenblum & Susan Maples: «Contracts confidential: Ending secret deals in the extractive industries" – Executive summary, 2009, Revenue Watch.

The Transparency Agreement should generally not be applicable to the governing contracts, as these should always be transparent in order to promote a level competition among the companies, but to the extent that a country chooses, despite the benefits of contract transparency, to keep governing contracts confidential, then the tax administration should get these governing contracts from the relevant government counterparty.

As such it is possible to narrow and define the contract transparency under the Transparency Agreement to constitute detailed contracts with environmental and societal effects that are relevant for the tax assessment and all market contracts, inside or outside the country, that have fiscal consequences.

It also becomes possible to distinguish clearly between the parties that will publish the contracts:

- For license to operate and governing contracts it seems that the government is the more correct publishing party
- For detailed contracts and market contracts that fall under the Transparency Agreement, it becomes obvious that it is the company that needs to make the contracts transparent, and then only towards the tax authorities and other relevant authorities.

For the avoidance of doubt, the tax authority should have access to all contracts within a country that are relevant for the tax assessment. What we are talking about with respect to the Transparency Agreement, is that contracts that are part of the audit trail for revenues or costs that are outside of the company in the country, but inside the company group, are to be made accessible to the tax authorities on a sample-by-request basis.

6.5 Transaction transparency: Levels of transparency

When it comes to transaction transparency, i.e. transparency of individual transaction documents (not contracts), there are, in essence, three levels of transparency.

The highest level of transparency is between the industry and the government. This level is covered by EITI, which at its core is a reconciliation of taxes paid by the industry and taxes received by the government. EITI is fully voluntary and covers the complete tax payments of an industry within one country. It is the economic tax consequences of the transactions of the combined industry (all the companies in the country) that is in effect captured by EITI, and no documentation is released.

The second level of transparency is between the individual company and the investors and the society at large. This level is covered by the extended country-by-country reporting standard that is supposed to be enacted in law to make the competition among companies level. At its core is the reporting of tax payments in their natural context (investments, production, revenues, costs, employees). Extended country-by-country is supposed to be fully law-regulated and covers the complete tax payments by a company, country-by-country, presented in their natural context of key financial statement numbers. The economic tax consequences of the transactions in an entire company group (all the companies in the group) are, in effect, reported in an extended country-by-country reporting. No documentation is released.

The deepest level of transparency is between the individual company as custodian of natural resource revenues and the relevant tax authority or other relevant authority. This level is covered by the Transparency Agreement, and at its core lies a mother company guarantee, connected to the "license to operate", that no transactions will be routed through parts of the company structure that will claim confidentiality to any document that relates to transactions (revenues or costs) in a producing country. The difference between the other levels and this level of transparency is that (1) the transparency is done based on sampling, (2) documentation is released (3) the collection and release of documentation is based on a request by the tax authority or other controlling entity, and (4) the principles behind the sampling (how many samples per category per year) are agreed in connection with the mother company giving the Transparency Guarantee or entering into a Transparency Agreement and receiving the "license to operate".

Six questions arise:

1) Can the mother company give the Transparency Guarantee or enter into a Transparency Agreement on behalf of all the companies?

   There are several reasons why the mother company can give a Transparency Guarantee or enter into a Transparency Agreement on behalf of all the companies in the group:

   - Common ownership gives the mother company ownership rights to manage voting in the different board of directors in the group
   - Common top management installed by the Board of Directors gives the mother company management rights to lie down common principles that the entire group needs to adhere to
   - The top management has the responsibility to ensure that operations are done within the legal framework that the group operates within. A license to operate which includes a Transparency Agreement is part of the legal framework that the management must ensure is adhered to.
   - The management of the company within the country has an independent responsibility to ensure, together with the top management, that the transactions they carry out within the group are done with companies that will adhere to the Transparency Agreement/Guarantee. It is possible for both management teams, in case of doubt, to secure written agreements internally to secure the fulfillment of the Transparency Agreement.
   - Confidentiality is voluntary, which means that transparency is also voluntary. To the extent that the Transparency Agreement/Guarantee would include contracts that are confidential in agreement with other governments, our experience tells us that almost all, if not all, these contracts have clauses whereby disclosure as per legal requirements or requirements on par with law, like a license to operate, is fully acceptable, and disclosure to a tax authority is often exempted in its own right. This is always the case with contracts or documents between business partners.

2) What about joint ventures?

   In case the company within the country is a joint venture consisting of two or more independent owners (not within the same group), then all the involved groups would be included in the license to operate which means that all of them would also be included in the Transparency Agreement/guarantee, unless one party is the operator and only this party will have revenue and cost transactions between the company in question and the operator's group companies.

3) What sampling principles should be agreed in the Transparency Agreement?

   The sampling principles need to be dynamic, i.e. that the tax authorities ahead of the signing of any agreement (Transparency Agreement/guarantee vs license to operate) must have a clear view on how large a sample they need, depending on the number of transactions in each sampling category. The sampling principles can be set based on statistical measures, but normally this is a practice that the company's auditor does, based on the use of random sampling. A tax authority could use random sampling, but normally a tax authority would be interested in specific transactions based on a number of selection criteria like standard price (sampling) or deviating price (selection), standard volume (sampling) or deviating volume (selection), customer is either standard (sampling or selection) or non-standard (selection), etc. When allowed to sample, it is important that ALL the documents relating to a transaction be released, including all internal documents (agreements, transaction documents, supporting documents like memos, communication documents such as emails, etc.). This is because one is talking about internal transactions without negotiation elements in the traditional sense.

4) How far does the companies' information duty go (ref White Paper No. 25 (2012-2013)?

The information duty only goes as far as the sampling sizes agreed in advance in the Transparency Agreement. This is in order to protect the company against arbitrary sampling sizes, and provide predictability for both parties. These sampling sizes should be a standard measure based on the size of the business, predetermined by the tax authorities for any and all Transparency Agreements to be issued. There should be a reservation right in the Transparency Agreement that the sampling size can be changed if the methodology of the tax administration changes, but then all the Transparency Agreements change at the same time in order to avoid different treatment for different companies.

5) The information duty only goes as far as the first third party transaction outside of the group, unless, for purposes of convenience, there is like-for-like trading, under which circumstances the like-for-like product is sold to the first third party.

How far does the risk of sanctions go if undelivered (ref White Paper No. 25 (2012-2013)?

Violation of the Transparency Agreement should lead to sanctions if the company has access to the requested information. Sanctions must be proportionate, and could be tested legally – based on arbitral proceedings which do not involve secrecy jurisdiction. In extreme cases, a possible breach to the Transparency Agreement could include revocation of the extraction license (the license to operate).

In extreme cases related ONLY to the time involved before the release of the required documentation. The Transparency Agreement already includes the sampling size and that ALL documentation related to these samples needs to be released to the relevant authority in order to ensure that the authority gets the correct understanding of the transaction. Materiality is not relevant as all documentation has to be released for the sampled transactions, no exceptions (anything else would allow the company to not release some transactions that the tax authorities or other authorities desired information about).
The ultimate sanction is revocation of the license to operate. The transparency violation must, in this case, be both prolonged and very serious. Before one reaches this very serious sanction opportunity, there must be predictable sanction steps with proportionate sanctions in place. Examples of what these could be:

- A reasonable period for the company to produce the documentation: 4 weeks

- Overdue delivery: warning letter that in 1 month a fine will start running

- 1 month overdue: daily fines start running, increasing by month of non-delivery

- 3 months overdue: warning letter that in further 3 months an export embargo will be put into effect. The export embargo can be cancelled by the company by taking legal action that proves that (1) the documentation does not exist and the reasoning for this or (2) the company does not have access to the information or (3) the transgression by non-production of the documentation is minor (maximum impact assessment show potential assessment less than X% (one-digit number, for example 1 or 2 %) of the taxes estimated in based on the tax return) or (4) the tax authorities are outside their sampling size.

- 6 months overdue: export embargo is put into effect if not stopped by legal action. Warning letter that a process to revoke the license to operate will be initiated in another 6 months.

- 1 year overdue: process to revoke the license to operate is started. Process steps to revoke will depend on the legal system. Revoking of the license to operate can include expropriation, forced sale of the asset on behalf of the company or that the company itself is asked to sell the operation in confidentiality (in order not to impact the price) or forced transfer to another operator with or without compensation (depending on the seriousness of the transgression). The profit from any sale of the asset is taxable within the country regardless of other capital gain tax rules in the country.

These are just examples of actions. However, the timeline has been thought through with respect to a weighting of a company's ability to provide documentation and protection of the company in the short term versus the tax administration's (and the country's) need to resolve the issues in the longer term.

6) What happens if discrepancies are discovered in the disclosed documentation that lead to an assessment?

It is common practice to be able to increase the sample size if deviations are discovered that have material impact on the result of the first sampling. Procedures for this should be agreed in advance in the Transparency Agreement contract.

The answers to the six questions above clearly demonstrate that it is possible:

- for a company to enter into a Transparency Agreement with a government in exchange for the license to operate,
- to balance the risk picture between company and tax authorities (or other controlling institutions), and
- to make a Transparency Agreement predictable and legally testable.

This report highlights the opportunities and benefits for a country that wants to make use of the Transparency Agreement, while at the same time exploring the issues and threats to the company by entering into a Transparency Agreement (this chapter and chapter 8 below).

6.6 How can a Transparency Agreement be implemented?

6.6.1 Introduction

A Transparency Agreement should apply equally for all companies. It is up to the individual country to evaluate whether they want to do this through a model agreement or through law. The purpose of the Transparency Agreement falls short if it is made into a negotiable position between the authorities and the individual company, resulting in different demands for transparency from different companies. The intention is to create a more equal competition, not the opposite.

6.6.2 Prerequisites for implementation

All countries can introduce a Transparency Agreement as it is negotiated with each company.

Not all countries are in a position to introduce a Transparency Guarantee immediately. The reason for this is that the conditions differ among countries. Here we will just outline the prerequisites for implementing a Transparency Guarantee:

1) Understanding E&P companies

   Many countries are too lenient towards extractive industry companies, particularly mining companies. Marginal tax rates below 50% on extraction of non-renewable resources are probably too low. Then again, some countries have too high demands that are not realistic if one wants an optimal development of resources. Marginal tax rates above 80% are probably too high.

   It is necessary for governments to understand the priorities better when attracting/negotiating/dealing with extraction companies. Governments need to understand that when a company enters negotiations in order to enter a country, they have already assessed the country as a likely candidate. What governments need to do is to create equal terms under which different companies enter the country. If the terms are negotiable (the sampling size etc., not the transparency itself), every company will negotiate as fiercely as possible in order to secure that their competitors do not get more favorable terms than themselves.

   Companies will have a higher acceptance if the Transparency Agreement is a demand put on all companies. If the transparency itself is made negotiable, then all companies will try to negotiate it away. In cultures where negotiation is common, this will be interpreted as if all companies do not want the Transparency Agreement. However, it only means that any company will try to negotiate the best position possible. If you make something negotiable, you must expect that companies negotiate. However, the best companies are really best served if all companies, the best and the worst, have equal non-negotiable terms.

2) Geological prospectivity

   The only reason an extractive company enters a country is that it wants to increase its profits. It does that only to the extent that it discovers large commercial resources. When a company develops smaller resources, it is really only to recoup the exploration costs that it has incurred to find large deposits, as large deposits are few and far between. There is no reason to hide that what companies are after is the large deposits. A country with large structures that can contain large deposits has a high geological prospectivity. If a country knows that it has a high geological prospectivity, then the country is in a position to introduce a Transparency Guarantee. A country that does not know its prospectivity is in no position to introduce a Transparency Guarantee. High prospectivity (which translates to high "attractiveness") is a prerequisite for countries that want to be among the first to introduce the Transparency Guarantee.

   An alternative to high prospectivity is support by other countries, see 4) below.

3) Clear, consistent and communicated principles

   It is a definite prerequisite for introducing a Transparency Guarantee that the terms be very clear and unambiguous. The terms need to be applied consistently to all companies and they must be communicated ahead of any licensing round. That means that it should be part of the legal framework or be a non-negotiable part of a model agreement.

4) Support by other countries

   An alternative to high geological prospectivity is if a group of countries introduces the Transparency Guarantee simultaneously. This would effectively reduce the companies' ability to shop among different countries. An example is Africa. Africa is a highly prospective continent. However, not all countries have high prospectivity. One solution could be that the Transparency Guarantee was discussed and agreed in the African Union, and all countries in the African Union implemented the Transparency Guarantee reasonably simultaneously. Any extraction company that would like to have access to the resources of Africa would then be faced with the same demand, and African countries would be in more control of their own resources.

   One does not need as large a group of countries as the African Union though. Usually it will be enough to have neighboring countries that have formed alliances already. A long established organization like SADC, for example, would be enough. If you went all the way down to individual countries, this would be the same, for example, as South Africa demanded a Transparency Guarantee from their gold companies, because South Africa has high prospectivity in gold. It would not work to have South Africa demand a Transparency Guarantee in oil & gas, as South Africa is currently viewed as having low prospectivity in oil & gas. To the extent that South Africa wanted a Transparency Guarantee in oil & gas, then that country would have to seek support from other countries.

6.6.3 Implementation

The Transparency Agreement can easily be implemented country by country with each country having to make its own decision. However, the solution would probably be to introduce it:

- unilaterally by high prospective countries
- multilaterally by a group of medium prospective countries
- united through a common organization by countries that have varied or low prospectivity
- by associating a country with a convention developed through international organizations.

The Transparency Agreement is meant to be implemented at the same time as the license to operate. A company would thus not get a license to operate unless it accepts the Transparency Agreement at the same time. This would keep out of the country those extractive companies that are not willing to be transparent in their operations with the government, and would thus function as a screening tool between the good and the bad companies.

A Transparency Agreement needs to be restricted to samples though, as it would be too great a burden to have the Transparency Agreement cover all of the transactions. Samples will have to be drawn statistically or be selected based on certain criteria. Only to the extent that there are mistakes would it be relevant to draw an extended sample or, if the population is small, documents for the full population. We will, however, emphasize that the major goal is to gain access to all available and necessary information, not to gain access to a limited number of documents.

7. What may be positive and negative consequences?

7.1 Benefits

We listed ten arguments that generally mention the purpose and benefits of a Transparency Agreement. In more detail, there are a number of benefits associated with the Transparency Agreement/Guarantee:

- The purpose of a Transparency Agreement is that it ensures that documents relevant for the developing country's government become accessible as case documents, and that a potential dispute involve the interpretation of the documentation, not the obtaining (of the documents). This is an extremely central part of the Transparency Agreement/ Guarantee. Today countries are unable to access documents from other parts of a group operating within the country, or it takes lengthy and costly legal processes to access the documents. However, this is a wasteful use of money and legal systems. Any controversy should be about how the documentation should be interpreted, not which documents are available for the company and which are available for the government. If a dispute nevertheless arises with regard to a document that must be provided, then the arbitration must decide. The key principle must be that when the company's tax return is being assessed by the tax administration, the tax administration has had at least a possibility to sample the full documentation of the entire audit trail for revenues all the way to a third party buyer, and for costs all the way to a third party seller. Only then can a tax administration and a company interpret a common set of documents that builds up under an assessment of the company's tax return in the country. Today extractive companies can use secrecy mechanisms to hinder insight into the audit trail of revenues and costs to third parties, an absurd concept as it is the tax administration that is responsible together with the company to ensure the assessment of the company's revenues, costs and profits is correct.

- A Transparency Agreement can be a strong and clear position to promote "the best companies" to the detriment of "the worst companies". Therefore, when the host countries announce new oil concessions, it should be clearly stated that a Transparency Agreement is a significant element in the final decision on which company will be preferred. The worst companies are those that have no intention of abiding by the laws of the country and use all the tricks in the book to reduce their revenues and increase their costs in the host country, thus moving untaxed profits across borders, usually into a tax haven where there is no additional taxation. A company of this sort will normally not pay any taxes of substance in the host country, whatever prices there are for the commodity. The reason is that there is such an abundance of tax evasion techniques that a company essentially does not need to pay more taxes than they effectively want to if their tax morale is low or non-existent. A company of this sort will normally pay some taxes in order to avoid too much attention. A country will normally not discover this before the company has reached payback, i.e. the time when the investments have been paid back and they would normally show quite high profits. Many companies never reach this stage as they have no plans to pay taxes. This could take from 5 to 10 years, and in the meantime they have produced a major part of the resource. If they are in the "right" country, the company can at that point sell the assets and the resource to another company, and walk away with the sales profits untaxed unless the country has quite sophisticated capital gain rules. Some natural resources in the world will unfortunately have exactly this course of history. By introducing a Transparency Agreement/Guarantee, one is effectively filtering the worst companies out of the competition, leaving the companies that have better intentions for the resources and for the country. This is effectively a mechanism to prequalify companies for entering the country. Prequalification, albeit without Transparency Agreements, are already used in many countries, and the Transparency Agreement would just be one other element in such a prequalification.

- A Transparency Agreement will make companies more transparent towards host countries; it will make governments more transparent towards citizens. If a company chooses to not be transparent it will be very revealing. It means the company never had good intentions when it approached the country in the first place (or it is afraid of being discriminated against if the Transparency Agreement/Guarantee is negotiable).

- A Transparency Agreement can reduce the risk of secrecy, which allows for corruption and mismanagement. It is usually not the same people who make the laws that negotiate the deals with the extractive companies. A Transparency Agreement in return for a license to operate is thus a good governance instrument, whereby the regulators limit the worst companies and corrupt negotiation teams to enter into deals to the detriment of the country.

- A Transparency Agreement can reduce the power of the "facilitators" in facilitating secrecy. It is no secret that there is a whole industry consisting of solicitors, auditors and financial institutions associated with arranging the lowest possible taxation, whether it be corporate structures including tax havens, transfer pricing including fictitious elements and over-pricing, derivatives to move profits cross-borders, mark-to-market contracts that move profits outside the borders, etc. Creating equal competition is a vital element in ensuring that all companies are treated equally, and that all companies will have to abide by the same rules no matter how they are organized. The Transparency Agreement is one of the best guarantees for this.

7.2 Threats

A Transparency Agreement can obviously reduce some companies' desire to invest in the country, and would thus eliminate a certain type of company from entering the country. However, this is also a benefit, because it is not at all certain that a government would get any tax revenues of substance from this type of companies. Eliminating these companies from entering the country can actually be a revenue booster for the country in question. However, it does mean that some countries will have to search more for the good companies. For countries with low prospectivity this could mean the difference between finding resources in the first place and not finding them. Countries with low prospectivity can thus not introduce a Transparency Agreement/Guarantee before many countries with high prospectivity have introduced it (but they can still use the Transparency Agreement instrument). In the beginning, this is thus an instrument for high prospectivity countries or a group of countries interested in introducing the Transparency Agreement for the same commodity.

Lobbying is obviously a threat. Many of the worst companies will try to push industry organizations ahead of them in order to ensure that somebody else is working to ensure the Transparency Agreement/Guarantee is not introduced in countries. One must expect lobbying against such a mechanism. However, lobbying usually means that something is either working (and will have consequences for some companies) or it is an excessive mechanism (it will have a negative impact for all companies). An example of an excessive mechanism would be if the tax level is set too high. That is something that would lead to a negative impact that could mean that some discoveries were not developed under the current price expectations. The Transparency Agreement is not such an excessive mechanism as it is only targeting companies that have few or no intentions of creating cost-efficient operations that give a high taxable profit internally in the host country. If the Transparency Agreement becomes one of the mechanisms recommended in the Oil for Development program in Norway, that means that countries introducing it will have the support of at least one other country in utilizing the Transparency Agreement mechanism.

8. What may be a purposeful presentation of such an initiative?

Since not all countries have high prospectivity, a Transparency Guarantee initiative would have to be adopted unilaterally by one or several countries with high prospectivity, or by a group of countries for the same commodity, or all/enough resource-rich countries in a convention type of setting for all types of commodities. A Transparency Agreement initiative would be easier to introduce.

The easiest is if a group of countries, for example with the backing of the Norwegian Oil for Development program (as the initiative was introduced in Norway), would like to introduce a Transparency Agreement. The Transparency Agreement should probably first be presented in various tax administration fora in order to get support from various tax administrations that this is a mechanism that would give them a good tool they could utilize effectively, and cut costs in the processes of assessing extractive industry companies.

One way of presenting it is to make it a 6th element in the Task Force on Financial Integrity and Economic Development that was an initiative started by Norway. The extended country-by-country reporting and the Transparency Agreement/Guarantee are initiatives that are quite compatible. Extended country-by-country reporting promotes the good companies in the views of the investors that are investing their money in extractive industries, while the Transparency Agreement can keep out the worst companies from getting access to non-renewable natural resources.

A way to gain support for the initiative would be to create a roadshow and present it to many of the major civil society organizations in order to create awareness of the initiative and ensure that support is built around the same initiatives instead of different initiatives arising from different organizations, i.e. that civil society is speaking with one voice with respect to this.

9. To what degree can a Transparency Agreement give access to information that they would otherwise not have?

A tax administration will, under its own regulations, typically be able to access the contracts and the transaction documents that fall within its own jurisdiction. It will normally have to ask for, but cannot expect to get, contracts and documentation produced outside of the country for other legal entities within a company group. The Transparency Agreement ensures that a group of companies, before getting a license to operate, guarantee they will produce such contracts and documentation on transactions without delay when the tax authorities send the request (on a sample basis).

Today, tax administrations are wasting large amounts of money on chasing information from other countries, particularly from tax havens, or they are not making the effort because they do not prioritize the work due to cost-benefit evaluations. If they choose to initiate processes, they expect to have to spend a lot of time and resources following up on the information. This takes a number of years. The Anders Jahre tax case took 30 years to resolve including rounds in the judicial system. Many countries will not have the patience and the resources to enter into such lengthy processes with an uncertain outcome. These countries need more direct, cheaper and more efficient mechanisms to gather the information they need to form a good opinion on the appropriateness of the tax returns delivered by the companies.

10. Which legal considerations are important?

To what extent can a country impose sanctions?

Since the Transparency Agreement is attached to the license to operate, the ultimate legal consequence of not adhering to the Transparency Agreement would be withdrawal of the license to operate. However, there would have to be procedural steps before reaching this stage. What these steps might be would have to be decided within each country's legal system and framework. An example has been outlined in chapter 6.5.

To what extent does a company have the duty to provide information?

A company is defined as the operating company within the country in question and all its affiliated companies, up to and including the ultimate mother company. To the extent that it is a joint venture, affiliated companies would include all companies in participating groups that influence revenues and costs. The company's duty to provide information includes ALL information on SELECTED (sample) transactions for the entire audit trail of documents and contracts between a third party outside the company group and all the way to the company in the host country.

What is the duty to provide information of a company that is a part of the corporation but operates outside of the home jurisdiction?

The Transparency Agreement is given jointly by the operating company, its immediate mother company and its ultimate mother company. The Transparency Agreement includes a guarantee that no transactions will be routed through companies that will not adhere to the Transparency Agreement. Thus the duty of any company that participates in the audit trail of either revenues or costs is to provide the necessary documentation of contracts and transaction documents when being notified. A company would usually have this organized from a central place, for example where products are sold out of the group (a trading division/company) or a central procurement unit.

Attachment 1: Example of how a Transparency Agreement could be designed

The basic premise of the Transparency Agreement is that a company that has been GIVEN the right to extract resources from a country should IN RETURN ensure that the government authorities are able to extract the documentation necessary to correctly assess the revenue and cost transactions for taxation purposes, as well as ensure that other obligations (environmental, ethical, etc.) are fulfilled.
The Transparency Agreement can thus ensure that legal resources and money are not used to DOCUMENT revenues and costs, but rather that legal resources are used to INTERPRET the same documents.

A vital part of the Transparency Agreement is also to protect the type of companies that countries want to attract. Companies, however, also reap significant benefits from a Transparency Agreement:

- It will reduce the "race to the bottom" and thus protect companies that want to "play fair"
- It will increase investor faith in the companies when companies enter into a transparency agreement with governments, as the conflict level with governments is likely to be reduced
- It opens up the possibility of positive, long-term development in the countries, which actually gives the companies more stable framework conditions

Transparency Agreement - DRAFT TERMS

ARTICLE X Transparency Agreement

Article X.1 DEFINITIONS

Article X.1.1
"all necessary information" means all contracts, all documents and all other materials that are necessary to explain the transaction(s), whether produced physically or electronically and whether produced inside or outside [country], for the purpose of
(I) recognizing a revenue from petroleum activities or
(II) accepting a cost related to petroleum activities in the country.

"all relevant information" includes, but is not limited to, the following documents in addition to the basic documents:
(a) back-to-back documents which logically links two or more transactions; examples include, but are not limited to:
(i) a series of individual internal sales,
(ii) a sale (or a series of sales) and derivative agreements that are logically linked to the sale (or series of sales) as long as the derivative gain or loss is part of the tax base in the company in [country],
(iii) a series of individual cost transactions where mark-up is added to the cost base before the cost is accepted as a deductible cost in [country]
(b) preparatory documents that explain the purpose of the transaction, including relevant Minutes of Meetings, hereunder relevant minutes of meetings from the Board of Directors and relevant General Assembly protocols.
(c) supplementary documents that explain the treatment for accounting purposes in cases where accounting governs tax treatment or that explain the treatment for tax purposes where tax treatment is governed by separate rules, including auditor statements, letters and a request from the company to the auditor to share auditors work papers with the requesting party in [country].

Article X.1.2
"back-to-back documents" means documents that form the end of one set of a transaction chain and the beginning of the next transaction chain, where the transaction chains form a series of transactions that needs to be viewed in total in order to understand the full value of a revenue generated on the basis of production of petroleum in [country], or the cost structure of a cost accepted to produce petroleum in [country].

Article X.1.3
"company" means a company registered or incorporated under the [relevant act] of [country], and includes any affiliated companies as defined in [article].

Article X.1.4
"guarantee" means that the company will provide the requested information physically or electronically in [country] or will cover the travel expenses necessary for one set of travels of inspectors to review the material outside of [country].
"Guarantee/Agreement" further means that the company will not take legal action to prevent the release of the information, and will not invoke secrecy legislation in any nation to try to prevent the fulfilment of this guarantee.

Article X.1.5
"indirect transaction" means a share in a revenue or cost that is based on a pooling of underlying translations and an allocation of the combined revenues or the combined costs in the pool to separate entities within the group.

Article X.1.6
"legitimate" exit point is the LAST external revenue transaction (if there has been more than 1 in connection with the sale of a good or service involved)
"legitimate" entry point is the FIRST external cost transaction (if there has been more than 1 in connection with the purchase of a good or service involved)

Article X.1.7
"recognized authority" means, for the purpose of assessing the documents, the following government institutions in [country]:

Primary institution:
- Revenue Authority

Secondary institutions:
- National Bank
- Resource Ministry
- Ministry of Finance
- Economic Crime Unit

The government institutions can be amended by a 6-month notice to the company.

Article X.1.8

"requested" means that a written enquiry has been delivered to the company's registered address in [country]. It is the responsibility of the company to ensure that the enquiry is received by an authorized person within the company without delay.

Article X.1.9

"without undue delay" means that the company will provide the requested information within 4 weeks of request, after which penalties will apply by the day, unless a written extension has been requested and granted to the company.

Article X.2 TRANSPARENCY AGREEMENT

The Company has been given the right to extract petroleum resources under this Agreement. The Company in return guarantees that it will provide and make available all necessary information that is requested by a recognized authority in [country] for the purpose of assessing the profits and the losses for tax purposes or to ensure compliance with other rules and regulations without undue delay.

Article X.3 PURPOSE AND ACCESS

The purpose of the Transparency Agreement is to get the necessary information for the state involved to be able to assess the documentation for any revenue, cost transaction or any legal obligations following from relevant laws or regulations in [country]. The company thus guarantees:

(I) access, on a sample basis as defined in article X.6, to the entire audit trail of documents from the source state and all documents, including back-to-back documents, until there is a legitimate exit source of revenues or legitimate entry source of costs.
(II) access to financial statements for all the internal parties involved in the transaction trail
(III) access to list of ownership in any and all entities whether consolidated or not, including trustee positions and beneficiaries.

Article X.4 INDIRECT TRANSACTIONS

To the extent that there is no direct transaction, a state needs to gain access to the relative proportion of cost (or revenue) that has been allocated to the state comparable to the proportion of the same cost (or revenue) that has been allocated to other states, state by state.

The information on indirect costs (or revenues) must be supported by the principles used to allocate the revenue or distribute the cost.

Indirect transactions include, but are not limited to,

(a) Overhead allocations
(b) Marketing fees
(c) Technology fees
(d) Financial services
(e) Insurance services
(f) Brand and patent fees
(g) Research and development allocations
(h) Procurement and purchasing services
(i) Distribution services
(j) Manning services

Article X.5 AUDITOR CONFIRMATION

External auditor of the group accounts must, upon request, issue an attested confirmation that

(I) the financial statements disclosed to the state are the same financial statements that have entered the group's consolidated financial statements
(II) the released internal transaction information conforms to the eliminations in the group consolidation process
(III) the indirect transactions represent the full value of the revenue or the full value of the cost

Article X.6 FORM OF REQUEST AND RESPONSE (consider moving this to an annex and expanding upon it)

A request delivered in writing to the registered address of the company can take the following forms:

(I.a) identification of the source document that is the basis for the request or
(I.b) identification of the transaction that is the basis for the request
(II) the level of documentation required
  (a) audit trail of direct documents, contracts and financial statements only. Requests should be done on a sample basis where the population is large enough and the terms are standardized enough. It is the requesting party who decides what the sample size should be, but the company should be heard before requesting more than 10 audit trails from the same population. Examples of what would be the same population could be 10 identical audit trails for sales transactions from the same seller via the same channels to the same buyer.
  (b) item (II.a) above and in addition, back-to-back documents as defined in article X.1.1 (a). Requests should be made on a sample basis in line with (II.a) above.
  (c) item (II.a) and (II.b) above and in addition, preparatory documents as defined in article X.1.1 (b) and/or supplementary documents as defined in article X.1.1 (c). Requests should be limited to a minimum number of transactions. Information on large, infrequent transactions relative to the size of the normal monthly business can always be requested to the extent the requesting authority so determine.

Article X.7 RIGHT OF INSPECTION (review right of inspection in Audit clauses)

The state involved has the right to visit and inspect, on its own or by way of a third party, all premises involved in the audit trail to control the information given in relation to direct and indirect costs (or revenues).

The right to inspection applies irrespective of legal privilege and secrecy legislation in any jurisdiction, as long as the inspection is necessary to gain access to the information given to the state.

The company is committed to assisting the state and providing qualified personnel capable of fulfilling the obligation to provide the information needed.

Article X.8 DEFAULT

For the purpose of article X: If the company does not adhere to the transparency obligations, the state involved will have the right to start a process to terminate the extraction agreement with the company:

(I) After 4 weeks, or a later date until which the company has received written extension, there will be penalties, calculated by the day, of USD 1000, increased by USD 1000 for every succeeding week of non-delivery. 1 year of non-delivery will be regarded as default of the agreement, and the process will move to step (II).

(II) Upon non-delivery under X.8 (I) above, the state can cancel the agreement with 6 months' notice. The company can cancel the notice if it delivers the requested material within the timeframe of the 6 months' notice, unless the company has had 2 (two) previous non-deliveries under X.8 (I) under which circumstance the company loses the right to cancel the notice with a third delivery. Failure to comply with the 6 months' notice will move the process to step (III).

(III) Upon non-delivery under X.8 (II)

(i) the resource reverts to the government without compensation,

(ii) the infrastructure associated with the resource will be auctioned on the open market, and the company will receive a share of the proceeds, this being limited to the remaining tax value of the asset or the remaining loss carry forward, whichever is the largest. Any value over and above this share will, by default, revert to the government of [country]. The buyer can deduct the purchase price as his new asset value.

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