

November 16, 2017

The Rt. Hon. Greg Clark MP
Secretary of State for Business, Energy and Industrial Strategy
Department for Business, Energy and Industrial Strategy
1 Victoria Street
London SW1H 0ET
UNITED KINGDOM

Dear Secretary Clark:

We write to you to provide comment on your agency's review of the U.K. Reports on Payments to Government Regulators.

The Columbia Center on Sustainable Investment (CCSI), a joint center of Columbia Law School and the Earth Institute at Columbia University, is an applied research center and forum dedicated to the study, practice and discussion of sustainable international investment.

With this letter, we hope to share our research regarding the materiality of country by country and project by project extractives payment disclosure such as required through the United Kingdom's implementation of Chapter 10 of the the European Union Accounting Directive. We also provide references to investor comments, which reinforce the need for the global standard for payment transparency that the U.K. Reports on Payments to Government Regulators sustains.

When the European Union adopted the Accounting and Transparency Directives in June and October 2013 respectively, it greatly bolstered the reach of the decades-long effort to provide investors with material information regarding oil and mining project payments on a mandatory basis. As the UK Regulations, legislation in other EU Member States, Canada and Norway have come into effect the data necessary to assess non-technical risks, evaluate management strategies, and support efforts to hold resource rich country governments accountable finally have become available to investors and other stakeholders.

The attached submission made by CCSI to the U.S. Securities and Exchanged Commission (SEC) on October 25, 2015¹ outlines seven areas in which public payment data such as required by the U.K. Regulations may add material insight to investment analyses and improve investment environments. This research and its conclusions were endorsed explicitly in a March 6, 2016 submissions to the SEC made by investors representing more than US\$ 3.1 trillion in assets under management². In turn, the letter's arguments were referenced and examined in detail in the SEC's Final Rule issued on June 26, 2016³.

¹ Also referenced here: <https://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-93.pdf>

² ACTIAM NV et al. Letter Submitted to SEC Dodd-Frank Section 13(q) Final Rule Comment Process. March 6, 2016. <https://www.sec.gov/comments/s7-25-15/s72515-52.pdf>

"Finally, as the SEC evaluates the investor benefits of the proposed rule we recommend for your consideration the submission made by Jeffrey Sachs and the Columbia Center for Sustainable Investment (CCSI), which includes several clear demonstrations of the usefulness of the current Section 13(q) proposed rule in investment analysis for differing asset classes and methodologies."

³ U.S. Securities and Exchange Commission. Final Rule, Disclosure of Payments by Resource Extraction Issuers. p. 170-172. June 27, 2016. <https://www.sec.gov/rules/final/2016/34->

In the March 6, 2016 letter and many other submissions made to the SEC during the rulemaking processes for Section 13(q), investors emphasized the great importance of consistency in the disclosures required in all jurisdictions with extractives payment disclosures mandates. For example, a comment submitted by Calvert Investments (a subsidiary of Eaton Vance Corporation) on February 16, 2016 commends the Commission's decision to align the proposed rule's project definition with the EU Directives and the then draft Canadian definitions, which are based on payments resulting from a single contract, lease or similar agreement with a government. The letter goes on to state "consistency in (the project) definition between the EU Directives and the (then) draft Canadian definitions not only benefits investors seeking consistent disclosure, but also companies attempting to provide these disclosures efficiently and to achieve equivalency between disclosures required in different jurisdictions and through the EITI processes in which they may be engaged⁴."

The February 16, 2016 Calvert letter also includes a compilation of the 30 investor comments made to the SEC as of that date. These submissions include statements by diverse investors, which include the world's largest private wealth manager (UBS), the largest financial services conglomerate (Allianz), and the largest public pension fund in the U.S. (the California Public Employees Retirement System). Despite varying investment strategies and customers, these institutional investors share the message that the global standard of extractives payment disclosure, of which the U.K. Regulations are a critical part, provides material information and supports the stability required for investors to provide the capital necessary for our growing economies to meet the world's resource needs.

We commend your agency and the U.K. Government in general on its early and ongoing support of extractives payment disclosure. Further, we would welcome the opportunity to be of any assistance as you carry on your review of the U.K. Reports on Payments to Government Regulators.

Sincerely,



Perrine Toledano, Head: Extractive Industries, Columbia Center on Sustainable Investment



Nicolas Maennling, Senior Economics and Policy Researcher, Columbia Center on Sustainable Investment



Paul Bugala
Independent Investment Analyst

October 30, 2015

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Project level payment disclosure requirements by extractive industry companies as part of Section 1504 of the Dodd Frank Act

Dear Chair White and Commissioners:

The Columbia Center on Sustainable Investment (CCSI), a joint center of Columbia Law School and the Earth Institute at Columbia University, is an applied research center and forum dedicated to the study, practice and discussion of sustainable international investment. In this letter we express our professional opinion regarding the importance of project level payment disclosure by extractive industry companies for institutional investors. The findings presented hereafter are the result of a thorough investigation based on a myriad of interviews with active and passive institutional investors, as well as with academics in the economics, business and legal fields.

Background on Section 1504

The technical risks of global natural resource development have been well documented. What is less understood but no less important are the growing political, regulatory and reputational risks involved in meeting the world's increasing resource needs. Whether it is the threat of production disruptions in the Niger River Delta, nationalization or abrupt changes in tax policy risks in Venezuela, or a tenuous license to operate in Guatemala, country and project-specific non-technical risks are becoming more acute as companies push further into the frontiers of petroleum and mineral exploration.

To better assess non-technical risks, evaluate management strategies, and support efforts to hold resource rich country governments accountable, Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") requires the disclosure of tax and other payments to host governments by extractive industry companies listed with the U.S. Securities and Exchange Commission (SEC) on a project level¹. What must be disclosed includes the total amounts of the payments, by category; the currency used to make the payments; the financial period in which the payments were made; the business segment of the resource extraction issuer that made the payments; the government that received the payments,

¹ We understand the global standard for project level disclosures is consistent with the guidance initially set out in the August 2012 SEC Final Rules Section II.D.3.c. (Page 85-86), which indicate that project level disclosure is based on the contractual arrangements that define the relationship and payments made between companies and governments, and is reinforced in complementary laws such as the EU Accounting and Transparency Directives (<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32013L0034>, <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P7-TA-2013-262>), which define project as "the operational activities that are governed by a single contract, license, lease, concession or similar legal agreements and form the basis for payment liabilities with a government."

and the country in which the government is located; and the project of the resource extraction issuer to which the payments relate.

When the Dodd-Frank Act passed in 2010, its Section 1504 was a groundbreaking provision and served as a model for other countries to follow. However, while the law remains in place, the August 2012 rule implementing Section 1504 was successfully challenged by the American Petroleum Institute (API) and the U.S. Chamber of Commerce in 2013; accordingly, the courts have remanded the rulemaking back to the SEC. On October 2, 2015, the Commission released a rulemaking calendar that indicates it will draft a new proposed rule by the end of 2015 and meet to adopt a final rule in June 2016. Thus while a frontrunner in setting a new transparency standard in 2010, today the United States is lagging behind in regulating and improving good governance of the extractives industry. Investors will face incomplete and inconsistent payment reports until the SEC aligns its rules to the emerging global standard for payment transparency that it had originally conceived.² Further, given that other countries and companies are moving ahead with project level reporting, public mistrust may increase for U.S. listed companies that are not following similarly detailed reporting standards. This may increase political and social risks for investors that have shares in U.S.-listed companies.

Investor Involvement

For the past five years, investors with more than \$6 trillion of dollars in assets under management have written repeatedly to the SEC Chair and Commissioners in support of strong rules for the implementation of Section 1504. Among other benefits and considerations, they referenced “investors’ substantial interest in oil, gas and mining industry payment transparency.”³ They also underscored that the SEC’s August 2012 implementing rule “...would protect investors and promote efficient capital markets by providing investors with valuable factual information on risk profiles and company performance.”⁴

Presiding SEC commissioners and a former chair echoed these beliefs when the SEC issued its final implementation rules for Section 1504 in August 2012. For example, Commissioner Luis Aguilar stated plainly, “[t]he final rule we consider today is in the interest of investors.”⁵ Then Chairman Elisse Walter took this observation a step further by both pointing out how investors may use the information disclosed through the law and also by noting that the stability fostered by disclosures such as these contributes to more predictable investment conditions.⁶

Finally, many members of Congress including Section 1504 authors Senator Benjamin Cardin and Senator Richard Lugar have spoken on the Senate floor or submitted comments to the SEC stating that the legislative intent of the law is to provide necessary information to investors and

² For more information on trends in payment transparency, please refer to the appendix.

³ Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Group of institutional investors. August 14, 2013. <https://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-3.pdf>.

⁴ Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Group of institutional investors. April 28, 2014. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-36.pdf>.

⁵ U.S. Securities and Exchange Commission. Aguilar, Commissioner Luis A. “Facilitating Transparency of Resource Revenue Payments to Protect Investors.” SEC Open Meeting. Washington, D.C. August 22, 2012. <http://www.sec.gov/News/PublicStmnt/Detail/PublicStmnt/1370542580723>.

⁶ U.S. Securities and Exchange Commission. “Statement at SEC Open Meeting.” Commissioner Elisse B. Walter. Washington, D.C. August 22, 2012. <http://www.sec.gov/News/PublicStmnt/Detail/PublicStmnt/1370542577444>.

its rulemaking mandate is consistent with the Commission's obligation to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.⁷

Investor Benefits of Transparency

The following outlines six ways in which the presence and use of extractive industry payment information may improve investment environments and add material insight to investment analyses.

1. Help assess the effectiveness of the diversification of risks within a portfolio

Project level payment reporting helps deploy sound risk-diversification strategies where a key component of projects' costs (i.e: taxes, royalties or other payments) become known. The diversification of portfolios is the basic technique for risk management used by investors: a

⁷ Floor statement of Senator Lugar during Senate debate of the Restoring American Financial Stability Act. May 17, 2010. At 4:51:35 <http://www.c-spanvideo.org/videoLibrary/clip.php?appid=598156901>.

Floor Statement of Senator Cardin, "The Dodd-Frank Wall Street Reform and Consumer Protection Act". July 15, 2010. http://www.cardin.senate.gov/newsroom/statements_and_speeches/the-dodd-frank-wall-street-reform-and-consumer-protection-act.

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Benjamin Cardin, U.S. Senator, Maryland. December 1, 2010. <http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specializeddisclosures-94.pdf>.

Letter to Elizabeth Murphy, Secretary, U.S. Securities and Exchange Commission. Carl Levin, U.S. Senator, Michigan, February 1, 2011. <http://www.sec.gov/comments/s7-42-10/s74210-19.pdf>.

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Benjamin Cardin, U.S. Senator, Maryland; John Kerry, U.S. Senator, Massachusetts; Senator Patrick Leahy, U.S. Senator, Vermont; Charles Schumer, U.S. Senator, New York; and Barney Frank, U.S. Representative, Massachusetts. March 1, 2011. <http://www.sec.gov/comments/s7-42-10/s74210-42.pdf>

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Raul M. Grijava, Member of Congress, Tucson, Arizona. November 15, 2011. <http://www.sec.gov/comments/s7-42-10/s74210-120.pdf>.

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Benjamin Cardin, U.S. Senator, Maryland; John Kerry, U.S. Senator, Massachusetts; Senator Patrick Leahy, U.S. Senator, Vermont; Carl Levin, U.S. Senator, Michigan; and Charles Schumer, U.S. Senator, New York. January 31, 2012. <http://www.sec.gov/comments/s7-42-10/s74210-122.pdf>.

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Rep. Barney Frank, Rep. José E. Serrano, Rep. Norman D. Dicks, Rep. Henry A. Waxman, Rep. Maxine Waters, Rep. Donald M. Payne, Rep. Nita M. Lowey, Rep. Betty McCollum, Rep. Barbara Lee, Rep. Jesse L. Jackson, Jr, Rep. Alcee L. Hastings, Rep. Gregory W. Meeks, Rep. Rosa L. DeLauro, Rep. Marcy Kaptur, U.S. House of Representatives. February 15, 2012. <http://www.sec.gov/comments/s7-42-10/s74210-162.pdf>.

Statement of Senator Cardin at Senate Foreign Relations Committee Hearing on National Security and Foreign Policy Priorities in the FY 2013 International Affairs Budget. February 28, 2012. <http://www.sec.gov/comments/s7-42-10/s74210-262.pdf>.

Letter to Mary Shapiro, Chairman, U.S. Securities and Exchange Commission. Benjamin Cardin, U.S. Senator, Maryland; Richard Lugar, U.S. Senator, Indiana; Senator Patrick Leahy, U.S. Senator, Vermont; and Carl Levin, U.S. Senator, Michigan. October 31, 2012. <http://www.sec.gov/comments/s7-42-10/34-67717-comments-stay-motion/34-67717-comments-stay-motion-2.pdf>.

Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Senator Benjamin Cardin, Maryland et al. August 2, 2013. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-2.pdf>.

Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Senator Benjamin Cardin, Maryland et al. May 1, 2014. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-41.pdf>.

Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Rep. Maxine Waters, Member of Congress, et al. June 11, 2014. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-50.pdf>.

portfolio of different kinds of investments should yield higher returns and cause lower risks than any individual investment in the portfolio. However as highlighted by Robert F. Conrad in his August 17, 2015 submission to the SEC⁸ this diversification of risks is only effective when the assets within a portfolio are statistically independent. Project level information helps investors understand the level of interdependencies among assets in a portfolio. An equity analyst asked to evaluate investment decisions, either prospectively or retrospectively, of a company with multiple extractive industry projects based on the overall cash flow, is faced with significant challenges. No understanding can be gained of either the contribution of any one project to the overall returns or the variation in benefits created by the contractual structure. Project level data will help in this undertaking “to either measure the overall ex post present value of the country’s assets or the incremental effects on the variation of returns.”⁹

2. *Help adjust assumptions on a major cost to the project: the taxes and other payments*

This can be illustrated with a very simple example of a hypothetical mining company that operates two mines in a country wherein all details related to production, cash costs, depreciation and financial expenses are known individually for both mines, but where only company-wide income tax data is available. In this case, estimating individual mine valuation would require extrapolation of taxes for individual mines by the equity investor.

The following table shows the free cash flow estimates of the two Mines A & B for the mining company, wherein no project level tax data is available in the absence of Section 1504. An equity analyst would usually assume the effective corporate income tax rate of 20 percent for both mines.

Details	Unit	Mine A	Mine B	Total
Copper	kt	200	100	300
Price	\$/lb	3.00	3.00	3.00
Revenues	US\$M	1,323	662	1,985
Cash cost of sales	US\$M	(794)	(276)	(1,069)
Unit cash costs	\$/lb	1.80	1.25	1.62
Cash Gross Profit	US\$M	529	386	915
SG&A + Other Operating Expenses	US\$M	(66)	(33)	(99)
EBITDA	US\$M	463	353	816
Depreciation	US\$M	(80)	(40)	(120)
EBIT	US\$M	383	313	696
Net financial expenses	US\$M	(100)	(50)	(150)
PBT	US\$M	283	263	546
Income Taxes	US\$M	(57)	(53)	(109)
Income Tax %	%	20%	20%	20%
Net Income After Taxes	US\$M	226	210	437
Capex	US\$M	(80)	(40)	(120)
Free Cash Flow	US\$M	226	210	437
All-In Sustaining Costs	US\$M	1,097	451	1,548
	US\$/lb	2.49	2.05	2.34

⁸ Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Prof. Bob Conrad. July 17, 2015. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-81.pdf>.

⁹ Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Prof. Bob Conrad. July 17, 2015. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-81.pdf>.

Assuming a 25 year mine life for mine A and a 10 year mine life for mine B, constant copper production and prices, and a real discount rate of 10 percent, gives a net present value (NPV) of \$2,261 million for Mine A and \$1,421 million for Mine B.

However, assuming a blanket income tax rate for all the mines in one country is too simplistic, as all projects are different in terms of fiscal regimes, geography, infrastructural improvement initiatives by the company, among others, which may entitle some projects for varied tax incentives relative to others. In some countries such incentives are included in contracts, which supersede the law and are mostly confidential. Contracts also often stipulate stabilization clauses, which freeze fiscal terms and therefore changes in the statutory terms do not affect those projects. Some resource rich countries explicitly state in the law that fiscal terms can be negotiated on a project-by-project basis and therefore the statutory terms also do not apply. In addition, multinationals use their worldwide corporate structure to practice transfer pricing and lower their taxable income, which in turn creates differences between the effective tax rate and the statutory level.¹⁰

In the presence of project level disclosure requirements, the same hypothetical mining company would disclose the true breakdown of the \$109 million tax payment between the two mines. An equity analyst would be able to use the effective income tax rate for the individual mines. This would give a more granular estimate of the free cash flows and thus NPV. Assuming that Mine A pays \$20 million and Mine B \$89 million the following table shows the free cash flow calculation estimates of the two mines.

Details	Unit	Mine A	Mine B	Total
Copper	kt	200	100	300
Price	\$/lb	3.00	3.00	3.00
Revenues	US\$M	1,323	662	1,985
Cash cost of sales	US\$M	(794)	(276)	(1,069)
Unit cash costs	\$/lb	1.80	1.25	1.62
Cash Gross Profit	US\$M	529	386	915
SG&A + Other Operating Expenses	US\$M	(66)	(33)	(99)
EBITDA	US\$M	463	353	816
Depreciation	US\$M	(80)	(40)	(120)
EBIT	US\$M	383	313	696
Net financial expenses	US\$M	(100)	(50)	(150)
PBT	US\$M	283	263	546
Income Taxes	US\$M	(20)	(89)	(109)
Income Tax %	%	7%	34%	20%
Net Income After Taxes	US\$M	263	174	437
Capex	US\$M	(80)	(40)	(120)
Free Cash Flow	US\$M	263	174	437
All-In Sustaining Costs	US\$M	1,060	488	1,548
	US\$/lb	2.40	2.21	2.34

¹⁰ Given the contract specific fiscal regime the transfer pricing rules might be different; e.g. allocations for head office expenses might vary by contract which in turn changes the effective tax rate.

Using the additional income tax input data the above example provides an NPV estimate of \$2,626 million for Mine A and \$1,174 million for Mine B.

The comparison of NPV estimates of the two mines, as well as the overall company are summarized in the table below. It is clear that with project level income tax reporting, Mine A is now valued 16 percent higher and Mine B is valued at 17 percent lower. The distribution of free cash flow between the two mines increases the overall valuation of the company by 3 percent.

US\$M	Without	With	% Variation
Mine A	2,261	2,626	16%
Mine B	1,421	1,174	-17%
Total	3,682	3,800	3%

3. *Help assess the exposure to commodity price downturns*

Another way investors may use the project level payment data is to analyze the industry cost curves to forecast commodity prices. Using the above example, the all-in sustaining costs (AISC = production costs + operating costs + financing expenses + taxes and related payments + capital expenditure) estimates for the two mines used in the previous example also change with the income tax disclosure. The results are summarized in the table below:

US\$/lb	Without	With	% Variation
Mine A	2.49	2.40	-3.3%
Mine B	2.05	2.21	8.1%
Total	2.34	2.34	0.0%

Without project level disclosure, an investor would underestimate the AISC of mine B by 8.1 percent and conclude that the cost curve is steeper than it actually is. With a more accurate picture of cash costs for individual mines, investors have a way to identify which mines/projects would be more susceptible to declining commodity prices, and thus can allocate the investment dollars more efficiently. Commodity price declines play an important role in management decisions, such as project write-downs and closures that can have a very significant impact on future cash flows and equity valuations.¹¹

Additionally, with project level disclosure, we can assess the elasticity of Mine A and B's cash flows to prices. For instance, if Mine B has a more elastic tax regime with respect to prices than Mine A (and therefore a more elastic AISC overall)¹², taxes for Mine B will fall by relatively more than for Mine A in case of a price downturn. This means that in the case of Mine B, the state's risk sharing is greater and that of the investor is smaller. Project level disclosure will provide the information necessary to understand the relative risk sharing for various projects.

¹¹ See for instance: [BHP Billiton](#) writing down \$2.8 billion off the value of its U.S. onshore oil and gas business; [Anglo American](#) writing down \$4 billion of a Brazilian iron ore mine and a number of Australian coal assets (Tim Treadgold, "Widespread Mine Closures To Follow The Commodity Price Collapse", *Forbes*, July, 21, 2015. <http://www.forbes.com/sites/timtreadgold/2015/07/21/widespread-mine-closures-to-follow-the-commodity-price-collapse/>); Glencore's market capitalisation is down from \$60bn as compared to four years ago (David Sheppard, Neil Hume and James Wilson, "Glencore shares tumble on concerns over commodity prices," *Financial Times*, September 28, 2015. <http://www.ft.com/intl/cms/s/0/2eea3106-65c2-11e5-9846-de406ccb37f2.html#axzz3p5WJl64>).

¹² For instance Mine B has a sliding scale royalty according to prices whereas Mine A has a fixed royalty, irrespective of prices. In case of a significant price decline, Mine B is likely to pay a lower royalty rate than Mine A if the sliding scale thresholds were set appropriately. The same reasoning will apply to all price-indexed progressive fiscal regimes such as windfall taxes, resource rent taxes, price or profit based-sliding scale profit oil and cost oil, etc.

4. Lower the cost of capital

Studies have shown that companies that disclose earnings and tax payments outperform their peers that are less transparent. For instance, Barth et al. (2013) provide evidence that firms with more transparent earnings enjoy a lower cost of capital. They find “a significant negative relation between our transparency measure and subsequent excess and portfolio mean returns, and expected cost of capital, even after controlling for previously documented determinants of cost of capital.”¹³ In 2006, Leuz and Hail showed that the cost of capital for firms in countries with securities regulations ranking in the bottom quartile in terms of disclosure requirements was associated with a two percentage point increase as compared with the cost of capital for firms in countries whose securities regulation ranks in the top quartile.¹⁴ The lower cost of capital is the result of equity holders and investors granting more trust to the companies they are investing in.

This trust might be warranted: In 2011, CCSI showed that 17 publicly listed extractive industry companies that disclosed tax payments on a country-by-country basis financially outperformed (in terms of price earning ratio, return on equity, return on invested capital) and reported fewer incidences of human and environmental rights violations in the communities they were operating than companies that did not.¹⁵

5. Lower political risk

The perception of corruption, good governance and transparency are fairly well established considerations in the assignment of sovereign debt ratings. For example, the S&P Sovereign Government Rating Methodology and Assumptions, includes a political score, which considers the “transparency and accountability of institutions, data, and processes that also accounts for the perceived level of corruption of the country itself.”¹⁶

Evidence suggests that EITI implementation and compliance have become leading indicators of substantive efforts to reduce political risk and enhance stability in the eyes of the main credit rating agencies. For example, in October 2013, the credit rating agency, Moody’s, referenced the approval of Senegal’s EITI candidacy as a “credit positive.”¹⁷ In its note on the development, Moody’s noted the following:

[Senegal’s EITI candidacy] is credit positive because it reinforces Senegal’s commitment to improve transparency and governance, strengthens the predictability of the operating environment in the extractive sector, and promotes exploitation of the country’s resources, all of which will support the country’s future growth prospects and the

¹³ Mary E. Barth, Yaniv Konchitchki and Wayne R. Landsman, *Cost of capital and earnings transparency*, *Journal of Accounting and Economics*, Volume 55, Issues 2–3, pages 206–224, April–May 2013.

¹⁴ Christian Leuz and Luzi Hail, *International Differences in the Cost of Equity Capital: Do Legal Institutions and Securities Regulation Matter?*, *Journal of Accounting Research*, Volume 44, Issue 3, pages 485–531, June 2006

¹⁵ Letter to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission. Vale Columbia Center on Sustainable International Investment. December 16, 2011. <http://www.sec.gov/comments/s7-42-10/s74210-115.pdf>.

¹⁶ Allianz. Interview with David Diamond. October 11, 2013.

https://www.allianz.com/en/press/news/company/point_of_view/news_2013-10-11.html/.

¹⁷ Moody’s Investors Service, Inc. “Issuer Comment: Senegal’s EITI Candidacy Status Approved, a Credit Positive”. October 25, 2013. http://www.alacrastore.com/moodys-credit-research/Senegal-s-EITI-Candidacy-Status-Approved-a-Credit-Positive-PBC_159679#sthash.1OG03a9s.dpuf.

*government's creditworthiness. Adopting EITI standards will provide a more predictable operating environment in the natural resources sector.*¹⁸

Similarly, in May 2010, the credit rating agency Fitch raised Azerbaijan's Issuer Default Ratings (IDRs) to 'BBB-' from 'BB+' and its rationale featured the benefits of EITI on investor confidence prominently.

These are only two of the many examples that suggest that the participation in EITI and the accompanying improvements to transparency and good governance can have positive effects on the investment environment of countries and their sovereign debt.

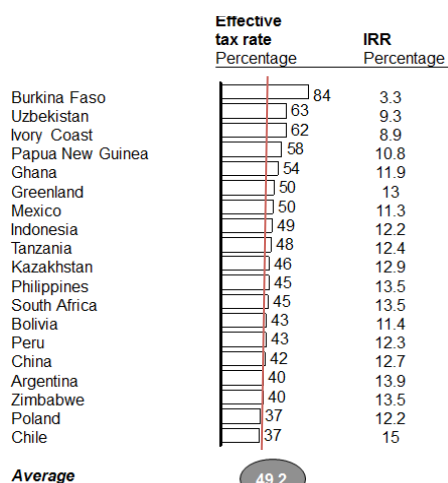
However, this benefit is limited to countries in which EITI implementation is politically feasible. Unfortunately, the limits of EITI's reach deprive investors of important data and indicators of investment stability and creditworthiness in many countries where improvements in governance are likely to be material considerations.

Of the 15 countries assigned a "failing" score in the Natural Resource Institute's 2013 Natural Resource Governance Index only three are EITI compliant (Cameroon, the Democratic Republic of the Congo, and Mozambique). None of the others assigned "failing" scores are currently even candidates for EITI implementation.¹⁹

Investors in sovereign debt may simply choose to avoid exposure to countries with high political risk indicators or poor credit ratings. However, investors in the securities of natural resource companies with portfolios that have exposure to the same countries may not have this option. Prompt implementation of Section 1504 would fill these critical gaps in investor's understanding in countries where payment transparency is most critical.

6. Better understand the risks of fiscal regulatory change

IRR and ETR for a Model Copper Mine in Selected Countries (Source: James Otto, 2006)



The knowledge of actual payments can help assess the Government Take or Effective Tax Rate (ETR), which is the total government payments divided by the pre-tax profit. Assuming production, prices, cash costs, capital expenditure, and financial expenses are known to the investor, project level payment disclosure provides information necessary to compute the numerator.

Knowing the Government Take will enable the ranking of projects extracting the same commodity and situated in a group of peer countries (those with similar geology, infrastructure and political risks). For each of those projects, both the Government Take and the project Internal Rate of Return (IRR) may be computed as shown in the figure to the left. If the

¹⁸ Ibid.

¹⁹ Natural Resource Governance Institute. 2013 Resource Governance Index. <http://www.resourcegovernance.org/rji/report#fig1>.

Government Take is far below average while the IRR is far above average, there may be pressure to renegotiate the contract or to revise the fiscal regime.

7. Help solve the principal – agent problem

When a capital provider invests in an extractive company, he or she is the principal and the company is the agent. As an agent, the extractive company must maximize returns for a given level of risk in accordance with the company's strategy. The investor must carry out due diligence to ensure that the company behaves accordingly and in line with what is reported. Transparency of payments at the project level provides additional information useful for investors to monitor companies' behavior and profitability.

In sum, we commend the SEC on its diligence in reflecting the needs of investors in its implementation rules for Section 1504. It is our hope that these examples highlight the usefulness of transparency to both active and passive investors and why it is of utmost importance to maintain company-specific, project level payment disclosure when issuing new rules to create improved efficiency in the capital markets. Furthermore, as outlined in the appendix, project level reporting is becoming the new standard. Not aligning the transparency rules to this standard would make it more complicated for investors to assess and compare the oil, gas and mining companies in their portfolios.

We would welcome the opportunity to discuss these issues further at your convenience.

Sincerely,



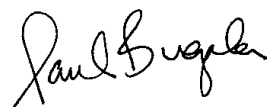
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APPENDIX

Mandatory and voluntary disclosure of project level tax payment data

Since July 2010, the European Union, Norway and Canada have adopted laws similar to Section 1504 of the Dodd-Frank Act, requiring project level payment reporting, and Australia introduced such a bill into the Senate in October 2014. The Extractive Industries Transparency Initiative's (EITI) new standard, introduced in July 2013, also includes revisions that require consistency with the U.S. and EU mandatory reporting laws in the area of project level disclosure. Several forward looking oil, gas and mining companies have already embraced voluntary project level payment reporting including BHP Billiton, Kosmos Energy and Tullow Oil (of which Kosmos Energy, BHP Billiton and Rio Tinto are listed on a U.S. stock exchange).

These developments suggest that the SEC would be making a mistake if it did not use the global standard for project level payment disclosure in crafting the new Section 1504 implementation rule. Different standards will make reporting more complex and costly for cross-listed companies. These companies include at least 22 of the global top 100 oil and gas companies and 25 of the global top 100 mining companies.²⁰ Similarly, different reporting standards would make it more complicated for investors to assess and compare the oil, gas and mining companies in their portfolio.

European Union

The EU adopted the Accounting and Transparency Directives in June 2013. The Accounting Directive requires large oil, gas, mining, and logging companies that are registered in Europe to annually disclose any payments above €100,000 to governments on a project-by-project basis. The Transparency Directive requires the same of all extractives companies listed on an EU-regulated exchange, no matter the company's size. A project is defined as "the operational activities which are (a) governed by a single contract, license, lease, concession or similar legal agreement and (b) form the basis for payment liabilities with a government". The Directives recognize as "equivalent reporting requirements" those in non-EU countries that have been assessed by the European Commission as being equivalent in accordance with article 47.

Member states were given a deadline to enact the Accounting Directive into national law by the 20th of July 2015, and the Transparency Directive by November 2015. This foresees the first reports being published in 2016 for the previous calendar or financial year. As part of its commitment to the G8 Presidency to "demonstrate....commitment to the global company transparency agenda"²¹ the UK was the first country in the EU to pass government regulations following the Directive on November 28, 2014. The first reports under the UK rules will be available for the 2015 financial year.

²⁰ Publish What You Pay (2015). Transparency on the Move: Payment Disclosure by the World's Largest Oil, Gas & Mining Companies. <http://www.publishwhatyoupay.org/pwyp-resources/transparency-on-the-move-payment-disclosure-by-the-worlds-largest-oil-gas-mining-companies/>.

²¹ Publish What You Pay (2015) Fact Sheet: UK implementing regulations and rules for reports on payments to governments (EU Accounting and Transparency Directives). http://publishwhatyoupay.org/sites/publishwhatyoupay.org/files/PWYPUK_fact_sheet_UK_regulations&rules.pdf.

Norway

Norway's parliament approved legislation requiring project level reporting of oil, gas, mining, and forestry companies in December 2013. No country-based exemptions are allowed and the requirements are effective for the fiscal year of 2014 with the first reports for 2015 already available.

Canada

In Canada, the Extractive Sector Transparency Measures Act received royal assent on December 16, 2014 and was passed into law on the 1st of June 2015. It follows the EU Directives closely. One of the major differences to the EU Directives is that the reports require attestation by a director or officer, or an independent auditor or accountant, to confirm that the information in the report is true, accurate and complete. Fines for non-compliance can reach up to \$250,000CAD.

Australia

On October 28, 2014, the Corporations Amendment Bill was introduced into the Senate, which foresees amending the 2001 Corporate Act requiring Australian extractive and logging companies to disclose any payments made to foreign governments over A\$100,000 on both a country-by-country and project-by-project basis. It also foresees for the Australian Securities and Investments Commission to publish the Publish What You Pay reports on their website within 28 days upon receipt. The bill still needs approval by both houses of the Australian Federal Parliament to become law.

Extractive Industries Transparency Initiative (EITI)

The EITI was launched in 2003 as a voluntary multi-stakeholder initiative for extractive industries bringing together governments, industries and civil society.²² In order to become a compliant country, among other things, companies have to report how much they paid to governments, and governments have to report how much they received. This allows a public reconciliation of accounts to assess whether any money went missing.

Revisions made to the EITI Standard in July 2013 aim specifically at ensuring convergence with the disclosure standard pioneered by Section 1504. Among these enhancements is the EITI Standard's requirement of project level disclosure "provided that it is consistent with the United States Securities and Exchange Commission rules and the forthcoming (sic, now implemented) European Union requirements."²³ The United Kingdom's implementation of the EITI standard is proceeding with implementation of project level reporting based on the EU Transparency and Accounting Directives (reporting templates for oil and gas²⁴/mining operations²⁵). In the past,

²² EITI History. <https://eiti.org/eiti/history>.

²³ EITI Standard. Section 5.2e. https://eiti.org/files/English_EITI%20STANDARD_11July_0.pdf

²⁴ UK EITI. "Final Reporting Template: Oil and Gas".

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/440677/Final_Reporting_Template_Oil_and_Gas.xls.

Burkina Faso, Indonesia, Mali, Timor-Leste and Zambia have either explicitly or effectively already required project level reporting.

In April 2014, a group of investors involved in EITI and representing more than \$6 trillion in assets under management wrote to the SEC pushing it to issue rules for the implementation of Section 1504 promptly and noting that “mandatory project- level reporting provision contained in Section 1504 as entirely consistent with, and complementary to, the goals of the EITI²⁶.”

Reporting by Companies

Statoil

In 2015, Statoil published all payments, equal or exceeding NOK800,000²⁷ on a project level basis (bonuses, fees and royalties) or entity basis (income tax). It also published payments to the Angolan government, which is one of the countries that the American Petroleum Institute (API) argues has laws in place that make publicizing revenue and government payment data illegal.

Statoil has stated it “welcome[s] initiatives to strengthen revenue transparency legislation, including project level disclosure of payments, as laid out in the EU Transparency Directive and in the Norwegian transparency rule... a global standard for revenue disclosure would be even more welcome.”²⁸ In 2013, the company also permitted the disclosure of correspondence that states: “Statoil has not supported the lawsuit initiated by API; in fact, Statoil has explicitly withheld.”²⁹

Rio Tinto

In 2015, Rio Tinto published its fifth voluntary tax payment report, which includes tax payments by business units. Many of the business units are individual projects, which also allows for the assessment of corporate income tax payments on a project level basis.

In the report, Rio Tinto states: “While we support transparency in reporting of tax payments, we are concerned about the proliferation of such new initiatives. Potentially we will face multiple and inconsistent reporting requirements, and will incur significant additional costs...We therefore believe governments should work together to adopt a consistent global approach, which establishes disclosure requirements and thresholds that are proportionate.”³⁰

Tullow Oil

In 2015, Tullow Oil released its second annual report, which complied with the EU Directives and UK regulations on mandatory disclosure on a project-by-project basis. The company also

²⁵ UK EITI. “Final Reporting Template: Mining and Quarrying”.

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/440675/Final_Reporting_Template_Mining_and_Quarrying.xlsx.

²⁶ Letter to Mary Jo White, Chairman, U.S. Securities and Exchange Commission. Group of institutional investors. April 28, 2014. <http://www.sec.gov/comments/df-title-xv/resource-extraction-issuers/resourceextractionissuers-35.pdf>.

²⁷ Slightly less than US\$100,000 as of September 28, 2015.

²⁸ Statoil (2015). 2014 Payment to governments.

²⁹ Letter from Baiba Rubesa, Vice President, Corporate Social Responsibility, Statoil. February 5, 2013.

<http://www.globalwitness.org/sites/default/files/library/Statoil%20Letter%20to%20Global%20Witness.pdf>.

³⁰ Rio Tinto (2015). Taxes paid in 2014: A report on the economic contribution made by Rio Tinto to public finances

provided additional voluntary disclosures on VAT, stamp duty, withholding tax, pay-as-you-go payments and other taxes.³¹ Tullow Oil's Group Vice President for Safety, Sustainability and External Affairs in October 2014 stated "[o]n the question of whether there have been any negative repercussions, the short answer is no. It hasn't cost us a lot of money and, candidly, both in the countries in which we operate and others, we haven't had negative repercussions."³²

Kosmos Energy

In 2015, New York Stock Exchange-listed Kosmos Energy voluntarily disclosed its contracts, agreements and 2014 payments to governments at the project level and on a disaggregated basis, ahead of any legally-mandated deadline to do so. Kosmos' belief is "that this type of disclosure is beneficial to investors, civil society, and local communities, and reflects evolving international expectations."³³

³¹ Tullow Oil PLC (2015). 2014 Annual Report and Accounts. Page 169. http://www.tulloil.com/Media/docs/default-source/3_investors/2014-annual-report/tullow-oil-2014-annual-report-and-accounts.pdf?sfvrsn=4.

³² Comments by Sandy Stash, Group Vice President for Safety, Sustainability and External Affairs, Tullow Oil. October 9, 2014. <http://www.resourcegovernance.org/news/october-9-washington-power-data-transform-natural-resource-governance-and-drive-economic-develo> at 1:00:14.

³³ Kosmos Energy. "Transparency." <http://www.kosmosenergy.com/responsibility/transparency.php>.