

EXPLANATORY MEMORANDUM TO
THE REPORTS ON PAYMENTS TO GOVERNMENTS REGULATIONS 2014
2014 No. 3209

1. This explanatory memorandum has been prepared by the Department for Business, Innovation and Skills and is laid before Parliament by command of Her Majesty.

2. Purpose of the instrument

These Regulations implement part of Directive 2013/34/EU of the European Parliament and of the Council on the annual financial statements, consolidated financial statements and related reports of certain types of undertaking ('the Directive') which mandates all large or listed companies registered in the United Kingdom and active in the extractive industry to report the payments they make to governments world-wide. The instrument sets out the detail of the reporting requirements, and the penalties associated with any failure to report.

3. Matters of special interest to the Joint Committee on Statutory Instruments

None

4. Legislative context

4.1 The Regulations implement Chapter 10 of the Directive. A Transposition Note is attached as an Annex to this Memorandum.

4.2 Chapter 10 of the Directive is being transposed into UK law ahead of the transposition deadline of 20 July 2015. This is because as part of the UK's G8 Presidency in 2013, the Prime Minister committed to implement Chapter 10 of the Directive early in order to demonstrate the UK's commitment to the global company transparency agenda.

4.3 The political commitment to implement early is also the reason that Chapter 10 is being transposed separately from the rest of the Directive. The remainder of the Directive will be implemented through a further set of Regulations, which will amend the Companies Act 2006, and will come into force by the transposition deadline of 20 July 2015.

4.4 The Regulations have been drafted using copy out where appropriate. The main area where drafting is not copied out or very closely followed is on the penalty regime. The Directive requires that Member States provide for a penalty regime that is effective, proportionate and dissuasive, but is silent as to how this is achieved. The penalty regime is therefore based on those penalty regimes already existing in company law, i.e. based on a system of criminal enforcement. Prosecutions under the Regulations are required to be by or with the consent of the DPP or Secretary of State.

4.5 The proposal for a Directive of the European Parliament and of the Council on the annual financial statements and related reports of certain types of undertakings 16250/11 was submitted to the Commons and Lords Scrutiny Committees on 20 December 2011. The proposal was cleared by the Commons Scrutiny Committee in Report 50, Session 2012. The Lords Scrutiny Committee cleared the proposal on 24 July 2012.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

5.2 The UK Government is responsible for company law in England and Wales and in Scotland. The Northern Ireland administration has agreed that, while company law remains a transferred matter within the legislative competence of the Northern Ireland Assembly, the 2006 Act and associated legislation on companies and partnerships should apply to the whole of the United Kingdom.

6. European Convention on Human Rights

The Parliamentary Under Secretary of State for Employment Relations and Consumer Affairs has made the following statement regarding Human Rights:

“In my view the provisions of the Reports on Payments to Governments Regulations 2014 are compatible with the Convention rights.”

7. Policy background

What is being done and why?

7.1 The requirements of Chapter 10 of the Directive mandates that all large undertakings and all public-interest entities active in the extractive industry or the logging of primary forests to prepare and make public a report on the payments they make to governments world-wide. The intention is to give citizens of resource-rich countries the information they need to hold their governments to account.

7.2 The requirements relate to companies who operate in the extractive industries. This includes those engaged in the extraction of oil, mineral and gas and the logging of primary forests.

7.3 In line with the commitments in the 2013 Lough Erne G8 Leaders' Communique, the UK Government continues to highlight the need for common global standards in transparency reporting. As part of this agenda the UK has committed to implement the Extractives Industries Transparency Initiative (EITI). Project level reporting will provide greater insight into how the industry operates and the range of economic contributions that can result.

7.4 The undertakings that will be required to prepare and publish a report are defined in the regulations. The definition of large is determined by meeting two of three criteria in relation to balance sheet total, turnover or average number of employees. The definition of those companies caught who work in the extractives or primary forest sectors are defined in European Regulations.

7.5 Chapter 10 of the Accounting Directive requires companies to report payments made to governments. The Directive requires the disclosure of the total amounts paid annually to a government, whether this is in money or in kind, where the payment is of any of the following types:

- (a) production entitlements;

- (b) taxes levied on the income, production or profits of companies, excluding taxes levied on consumption such as value added taxes, personal income taxes or sales taxes;
- (c) royalties;
- (d) dividends, other than dividends paid to a government as an ordinary shareholder unless they are paid in lieu of a production entitlement or royalty;
- (e) signature, discovery and production bonuses;
- (f) licence fees, rental fees, entry fees and other considerations for licences and/or concessions; and
- (g) payments for infrastructure improvements.

The Directive does not require reporting of reserves.

7.6 Payments below the threshold of £86,000 (sterling equivalent of 100,000euros) do not have to be reported if the payment relates to a single obligation and is not part of any related series of payments. For example a single payment of £75,000 for a licence in a year would not be required to be reported, whereas a series of four quarterly payments of £25,000 for a single licence each would need to be reported in aggregate. Similarly a single tax payment of £75,000 would not be required to be reported, whereas if an additional payment for the same taxation obligations of £15,000 was paid in the same year then the total amount would have to be reported in aggregate.

7.7 Payments need to be included in a report where they are made to a national, regional or local authority of a country. The term 'government' includes a department, agency or entity that is controlled by the government authority.

7.8 The requirements in relation to the content of the report oblige the reporting entity to either attribute every payment to a project or disclose the payment at an entity level. A project is defined 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 to a government. If multiple such agreements are substantially interconnected, this should be considered a project.

7.9 Reporting entities are not required to disaggregate and allocate payments on a project basis where payments are made in respect of obligations imposed on the company at the entity level rather than the project level. Such payments may therefore be disclosed at the entity level rather than at project level.

7.10 Alongside reporting monetary payments the regulations require the reporting of payments in kind. A value must be attributed to the payment in kind. Where applicable the volume of any non-monetary item transferred to the government should also be included in the report. For example if a royalty liability was satisfied by the delivery of 1,000 barrels of oil, the report would need to allow both the monetary value of the oil and the volume delivered.

7.11 Companies will be required to report on payments to governments for financial years which begin during the year beginning 1 January 2015. This will mean that the first reports will be made available in 2016. Following responses to consultation, companies will have 11

months to submit their reports to Companies House who will make the information available on the public register.

7.12 The penalty regime is similar to others within the Companies Act. The aim of the penalty regime will be to seek compliance, therefore once Companies House become aware of a missing report or incomplete report the company will be asked to comply within 28 days or they will be asked to confirm that a report is not necessary, they have reported through a parent company or if an equivalence regime has been agreed, that they have reported somewhere else.

7.13 Failure to comply with the request for information may lead to a fine. Should a company fail to complete a report both the company and directors could be subject to a criminal conviction and either a fine or imprisonment. In order to ensure that a case brought against a company is not frivolous or vexatious and is in the public interest the Director of Public Prosecution or Secretary of State will consider the basis of the case before giving consent to go to court.

8. Consultation outcome

8.1 Throughout the negotiation of the Directive, the department informally consulted industry and civil society on the EU reporting requirements. Stakeholders were informed of policy developments and their views helped inform the negotiation process.

8.2 Formal consultation began in March 2014. The consultation period ran for six weeks and sought views on areas that were not already fixed by the Directive.

8.3 In total, 31 consultation responses were received and the department published all consultation responses on its website;

<https://www.gov.uk/government/consultations/extractives-industries-reporting-implementing-the-eu-accounting-directive>

8.4 All responses to the consultation whether industry or a civil society supported the aims of the directive and the benefits of increased transparency. On the individual issues raised there was a general split between industry and civil society organisations. On the whole industry felt that the UK should not implement the measures early.

8.5 Other issues raised by industry related to competition issues, conflicts of law and equivalence with other regimes – particularly the USA. The Directive does allow for equivalence with other regimes but it will not be possible to agree such equivalence until other countries such as the USA have their implementing regulations in place. The Directive does not allow Member States to waive the requirement for companies to report, even if the company believes that they will be breaking a law in another country.

9. Guidance

The Department for Business, Innovation and Skills has encouraged an industry-led approach to the development of guidance. Industry and civil society are working together to create

guidance that will give companies the information they need to deliver accurate and meaningful reports to the Registrar of Companies. This guidance does not preclude any further guidance from sub-sectors of the industries affected by the regulations. As part of the consultation we sought views on whether industry guidance was the best approach.

10. Impact

These regulations implement an EU Directive. However, the UK has taken the decision to implement to requirements early. Therefore the Impact Assessment considers the costs associated with the early implementation. A draft Impact Assessment was made available for comment alongside the consultation. Following closure of the consultation the Impact Assessment was revised. The final Impact Assessment is attached to these regulations, and has been agreed by the Regulatory Policy Committee.

11. Regulating small business

These Regulations apply to all large and listed extractive companies registered in the UK. Small companies may be impacted by the Regulations if they are listed on the London Stock Exchange or form part of a larger group that are required to report.

12. Monitoring & review

The EU Commission will review the Directive by 21 July 2018. In order to inform that review, the UK regulations also include a three year review clause. We would expect the UK review to inform the wider review by the EU Commission.

13. Contact

Maureen Beresford at the Department for Business, Innovation and Skills (tel: 020 7215 3342 or email: maureen.beresford@bis.gsi.gov.uk) can answer questions about this instrument.