

# Financial transparency and accountability in the extractive industry

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# *The paradox of plenty*

Around the world, the extractive industries generate billions of profits from resource-rich countries, yet paradoxically, the majority of citizens from these same countries live in dire poverty. Unlocking this paradox involves understanding and addressing a crucial link: how a lack of transparency and accountability in the payment and receipt of natural resource revenues encourages corruption and mismanagement by public and private officials, undermines good governance, and chokes off income that could help reduce poverty, fund basic needs, and spur economic growth and development.

# *The resource curse in Africa*

- Africa is a continent gifted with rich natural resources, and where the extractive industries are booming.
- Several countries have only recently discovered their reserves of oil, gas or minerals, while in others, such as Niger, Nigeria, DR Congo and Gabon, extractive activities have been taking place for a few decades.
- Increased global demand for natural resources, rising commodity prices and an increasingly attractive economic investment climate, have pushed the expansion of extractive activities in countries such as Burkina Faso, Mali, Guinea-Bissau and others.
- Used well, these resources can create greater prosperity for current and future generations; used poorly, they can cause economic and political instability, social conflict, poor governance and lasting environmental damage.

# ***Financial transparency (1)***

- This phenomenon, known as the ‘resource curse’, is mainly explained by the secrecy which has characterised the extractive sector:
  - 1. Money received by governments can be misused or embezzled instead of channelled to improve the lives of citizens.***
- Transparency of payments done by companies to Governments and of revenues of Governments is a necessary and crucial first step towards a more accountable system for the management of natural resource revenues. If companies disclose what they pay, and governments disclose their receipts of such revenues, then citizens in resource-rich countries will be able to compare the two and thus hold their governments accountable for the management of this valuable source of income.
- Revenue transparency will also provide key information to promote a democratic debate over the effective use and allocation of resource revenues and public finance in order to meet development objectives, improve public services, and redistribute income.

# ***Financial transparency (2)***

- 2. Countries may not get a fair deal for the value of their resources due to secret agreements, poor enforcement of the tax law or its abuse by unscrupulous companies.***
- In order to track whether countries are receiving what they are owed by companies and whether these amounts are fair, the following information is needed from companies for every country where they have commercial activities:
  - Profits, production volumes and sales, so that e.g. royalties payments can be understood.
  - Intra-group trade between subsidiaries and the parent company, to expose usage of tax havens.
  - Assets and staffing information, to throw light on the use of 'mailbox' companies in tax havens.

# *Financial transparency – Achievements (1)*

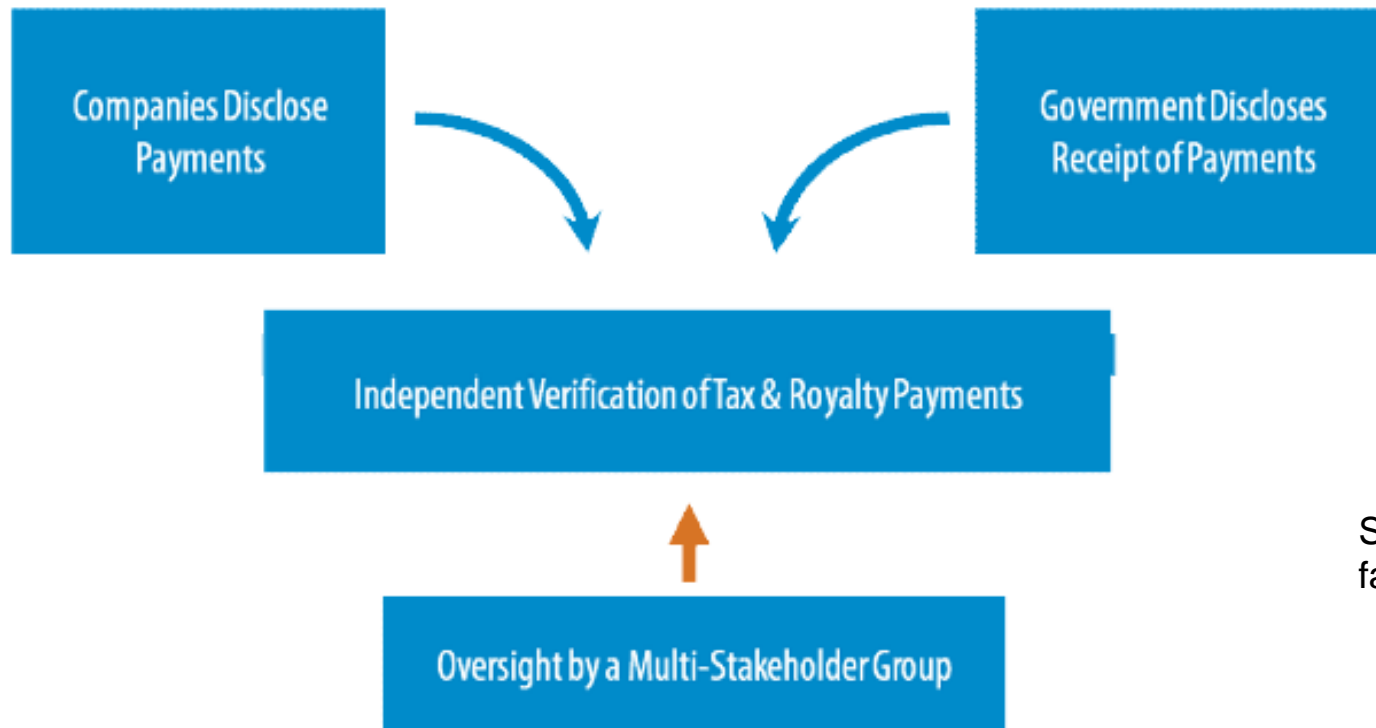
There is now wide international consensus in favour of increased transparency in the extractive sector as evidenced by, for example, the immense support from governments, companies, investors, financial institutions and civil society for the Extractive Industries Transparency Initiative (EITI)

Much of the progress that has been made is the result of multi-stakeholder efforts to promote revenue transparency throughout the world as part of the Extractive Industry Transparency Initiative (EITI). The EITI has been a groundbreaking initiative, and today, revenue transparency is generally accepted as a critical part of the governance package for nations to reap benefits from their natural resources.

# What is the 'EITI'?

- **A global standard for transparency in the extractives sector**
  - EITI involves the reconciliation of company payments with government receipts by an independent administrator and disclosure of that information to the public.
  - The objective of the EITI is to ensure that accurate figures about revenues are publicly available, to identify any potential discrepancies between payments & receipts and to investigate and address the underlying causes.
- **A voluntary, multi-stakeholder initiative**
  - The process is managed by government, company and civil society stakeholders. Civil society must be involved in the process

# What is the 'EITI'?



Source: EITI factsheet



## ***Financial transparency – Achievements (2)***

Currently, there are 21 African countries implementing the EITI, six of which have been declared compliant (Liberia, Ghana, Mali, Niger, Nigeria and Central Africa Republic); 19 African countries have started reporting revenues, many for the first time; and 39 EITI reports published by African countries are now available, more than half of which present disaggregated data.

## ***Financial transparency – Achievements (3)***

**The Dodd-Frank financial reform bill (2010)** in the United States -(provision 1504) requires all companies engaged in extractive activities listed on US stock exchanges to make annual public reports on the payments they make to governments of the countries where they have operations. Dodd-Frank 1504 adds to existing stock listing requirements in the US by obliging all extractive companies to publish the payments they make to the US and foreign governments in the countries where they operate.

# ***Financial transparency – Achievements (4)***



All companies that are listed in the US and engage in the commercial development of oil, gas and other minerals (defined as exploration, extraction, processing, export and other significant actions) will be covered. This includes eight of the ten largest mining companies and 29 of the 32 largest internationally active oil companies.

Companies that engage in the commercial development of oil, natural gas or minerals will have to report the type and total amount of payments made for each project, and the type and total amounts of payments made to each government. These payments cover report taxes, royalties, fees (including license fees), production entitlements and bonuses.

# *Financial transparency – Achievements (5)*

**Transparency and Accounting Directives of the European Union:** similar disclosure requirements are being introduced in the European Union. The EU Commission recently proposed amendments to the Transparency and Accounting Directives that will require all European Union-listed or large unlisted oil, gas, mining and logging companies to disclose their payments to all governments on a country by country and project by project basis.

These laws, once fully adopted and implemented, will result in disclosure of information which members of PWYP African coalitions will be able to use to hold their governments accountable.

# *Financial transparency – Achievements (6)*

- **National legislation** (Liberia EITI law, Nigeria EITI law, Ghana Petroleum Revenue Management Bill), constitutional reforms (Niger) also seeks to respond to this problem.
- Freedom of information laws have been adopted by a number of African countries (e.g. Liberia, Uganda, Nigeria) though in many cases implementation has been lacking. If implemented meaningfully these laws would equip the public with the right to information on the receipt and use of natural resource revenues.

# *Contract transparency (1)*

- Contract transparency is an essential precondition to ensuring that all parties benefit from the extractive industries. Disclosure is a necessary precursor for the coordinated and effective management of the sector by government agencies.
- The contracts between governments and oil, gas and mining companies are central to any effort to trace revenues and expenditures in the extractive industries. Extractive industries contracts determine the benefits, obligations and indeed the transparency of the agreements between countries and industry.
  - **The amounts that companies pay to Governments are usually a function of the fiscal terms contained in the contracts.**

# Contract transparency (2)

- **If citizens are to know whether payments and receipts from extractive companies reflect a fair deal for the country, the contracts on which they are based must be made transparent as well.**
- Contract disclosure will enable EITI implementing countries establish what the companies don't pay. In Ghana, the Multi-Stakeholder Group has mandated the EITI Auditor to reconcile payments with the fiscal terms contained in the mining contracts of EITI-participating companies.
- Liberia on the other hand has passed a contract disclosure Act, paving citizens' access to natural resource contracts.
- However citizens of most EITI implementing countries in Africa still do not have access to resource contracts that have been negotiated in their name.

# *Transparency of government expenditure*

- It is impossible to ensure proper management of natural resource wealth by looking exclusively at revenues. Transparent and accountable management and expenditure of public funds is essential to addressing the resource curse.
- Citizens in resource rich countries must have the data and the tools to assess the revenues flowing into their government's accounts. But the revenue information produced from exercises like the Extractive Industries Transparency Initiative (EITI) is only useful insofar as citizens and policymakers can use it to analyse the management, prioritization and spending of these funds for economic growth and human development.
- The adoption of revenue transparency standards in many countries has resulted in more data being produced and disclosed, and more demand for attention to government spending and development outcomes. Allocation, management and spending of these resources has to be grounded in principles of transparency, accountability and sustainability to produce sustained economic and social impacts.



# Challenges to citizens' engagement in extractive industry governance

## 1. **Free, full and independent participation of citizens:**

There are still many limitations to a free and meaningful engagement of civil society in the debate around transparency and accountability in the extractives sector: In several African countries, civil society advocates face harassment, intimidation and threats to their security that are directly linked to their advocacy for better transparency in the extractive sectors.

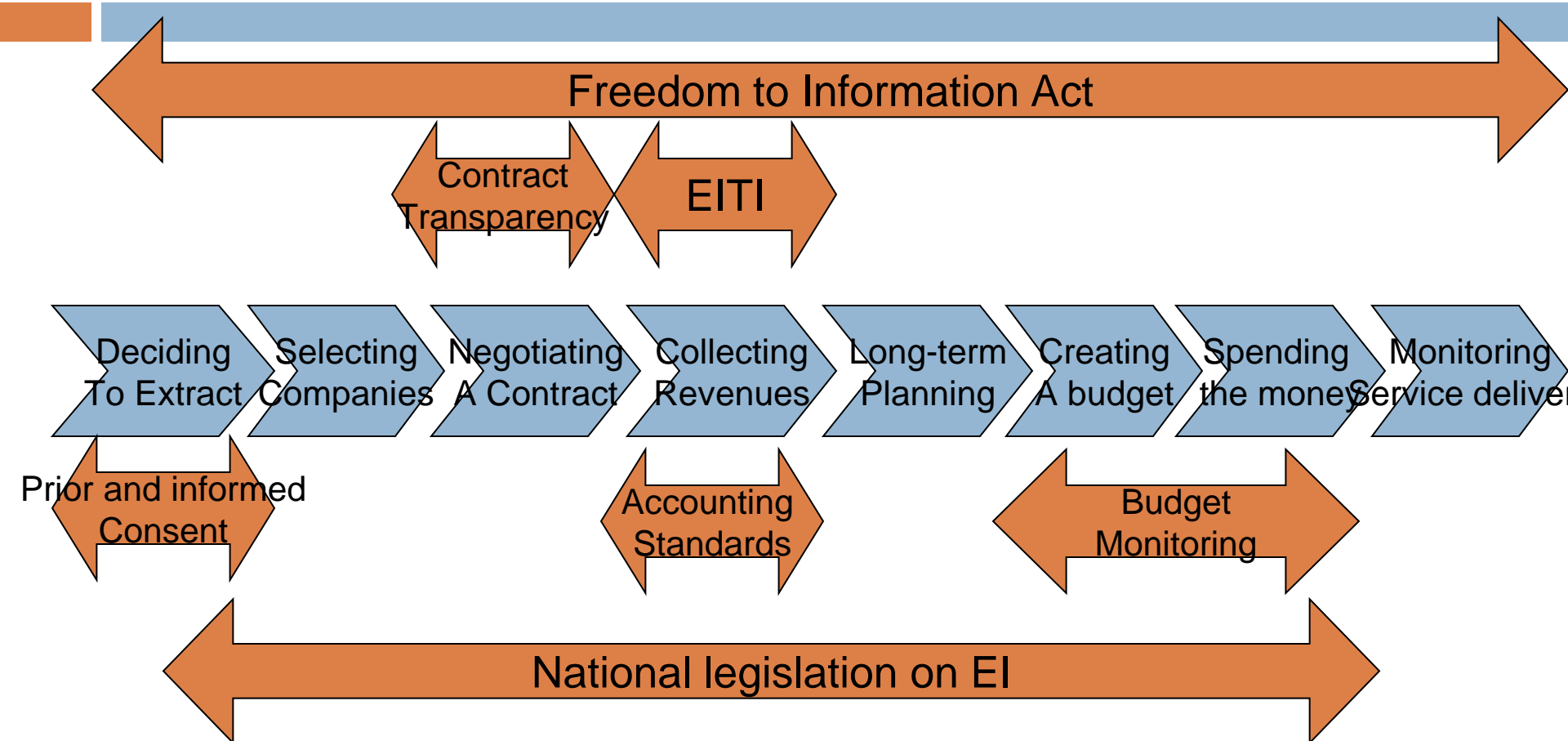
2. **Capacity constraints:** civil society and public sector still face capacity constraints that represent severe obstacles.

# Conclusions

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- Towards transparency and accountability
- True transparency and accountability throughout all the value chain of extractive industry.
- Despite the important achievements, there is still a lot to do to ensure that transparency is at the core of stakeholders' practices and legislative and policy frameworks that govern EI all over Africa.

# Transparency in the EI value chain



# Thank-you!

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# Transparency in the extractive industries

## The value chain approach:

As the transparency movement has evolved, there has also been growing recognition that extraction is a process comprised of a series of decisions – from the decision (or not) to extract), the licensing and contract agreements that determine how much is paid... down to the allocation and spending of the government revenues earned through these payments.

