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Court Vacates SEC Rule on Disclosure of Government Payments by Resource Extraction Issuers While Similar EU Requirement Is Finalized

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On July 2, 2013, a US court vacated the new SEC rule requiring resource extraction issuers to file annual reports with information about government payments for the commercial development of oil, natural gas or minerals. Meanwhile, a new EU accounting directive was finalized that imposes a similar disclosure requirement for large mining companies registered or listed on a regulated market in the European Economic Area.

District Court Vacates SEC Government Payments Rule

On July 2, 2013, the United States District Court for the District of Columbia (the "District Court") vacated Rule 13q-1 (the "Rule") under the Securities Exchange Act of 1934 (the "Exchange Act"). The Rule had been adopted by the Securities and Exchange Commission (the "Commission") in August 2012 pursuant to Section 13(q) of the Exchange Act, which was added by Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). The Rule adopted by the Commission required "resource extraction issuers" to file annual reports with information relating to any payments made by the issuer, a subsidiary of the issuer or an entity under the control of the issuer to a foreign government or the US federal government for the purpose of the commercial development of oil, natural gas or minerals, beginning with fiscal years ending after September 30, 2013. These annual reports, like other filings with the Commission, would be available to the public.

The American Petroleum Institute and others brought an action against the Commission challenging the Rule for a number of reasons. On a motion for summary judgment, the District Court determined that "the Commission misread the statute to mandate public disclosure" of each issuer's annual report. The Court also found that the Commission's

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decision to deny any exemption for foreign law disclosure prohibitions "was, given the limited explanation provided, arbitrary and capricious." Because the District Court found these to be "substantial errors," the District Court has vacated the Rule. Also, because of these two "substantial errors," the Court did not consider the plaintiffs' First Amendment challenge or their other Administrative Procedure Act challenges.

Because of the District Court's decision to vacate the Rule, the Rule as it now stands is void. Consequently, we believe the Commission will go through a new rule-making process to implement Section 13(q) of the Exchange Act, which requires the Commission to issue rules requiring resource extraction issuers to include in an annual report information relating to any payment by the issuer, a subsidiary of the issuer or an entity under the issuer's control to a foreign government or the US federal government for the purpose of the commercial development of oil, natural gas or minerals. Until a new rule is adopted by the Commission, issuers have no obligation to comply with Section 13(q) of the Exchange Act.

The District Court's decision does not affect the disclosure requirements under the conflict minerals rules adopted by the Commission pursuant to Section 13(p) of the Exchange Act, which was added by Section 1502 of the Dodd-Frank Act. The conflict minerals rules are also currently subject to a challenge in the District Court, and oral arguments in that case were held on July 1, 2013.

EU Requirement for Large Companies in the Extractive Industry to Disclose Government Payments is Finalized

On June 29, 2013, the text of a new EU accounting directive (2013/34/EU) that imposes a similar disclosure requirement for large mining companies was published in the EU Official Journal. The directive will apply to companies registered in the European Economic Area ("EEA"). EU Members States are required to implement the directive by July 20, 2015, such that it will apply to financial statements for financial years beginning on or after January 1, 2016. An equivalent requirement will, subject to certain applicable exemptions, apply to non-EEA registered companies with securities listed on any EEA regulated market, through amendments to the EU Transparency Directive (2004/109/EC) that are currently being finalized in Brussels.

The directive, which consolidates, repeals and replaces the Fourth and Seventh Company Law Directives (78/660/EEC and 83/349/EEC, respectively), requires "large undertakings" and "public-interest entities" that are active in the extractive industry or logging of primary forests to disclose annually, in a separate report from their annual report, all payments of €100,000 or more in that year to governments of countries in which they operate. "Large undertakings" are companies with any two of the following characteristics: a balance sheet over €20 million, a net turnover over €40 million and an average number of employees per financial year of more than 250. "Public-interest entities" are companies with transferable securities admitted to trading on a regulated market, credit institutions, insurance undertakings or companies designated as public

interest entities by an EU Member State by virtue of their business, size or number of employees. The new requirement covers any activity involving the exploration, prospection, discovery, development and extraction of minerals, oil, natural gas deposits or other materials. Moreover, it goes beyond the US rule to cover logging activities.

The disclosure must be categorized per project, and government and must include the types of payments comparable to those disclosed by a company participating in the voluntary Extractive Industries Transparency Initiative, such as payments for:

- production entitlements;
- taxes levied on income, production or profits;
- royalties;
- some dividends;
- signature, discovery and production bonuses;
- license fees, rental fees, entry fees and other considerations for licenses and/or concessions; and
- payments for infrastructure improvements.

In an accommodation presumably aimed at the US rules, the directive allows the European Commission to accept a company's report prepared pursuant to another country's comparable requirements, but only after the European Commission applies detailed evaluation criteria as to scope, level of detail and process.

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