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The EU's Transparency Initiative for Mining Industries— Right Direction, Insufficient Means

Lidia Puka

By obliging EU-registered companies that explore, develop or extract oil, gas, coal and other minerals to disclose payments made to governments, the European Union seeks to create a new tool of control and accountability. With amendments to its existing Transparency and Accounting Directives, the bloc thus hopes to bolster fair market rules, combat tax evasion and boost global governance. To achieve its high ambitions, however, the EU needs to learn from existing initiatives elsewhere and to minimise the burden on companies. It can do this by improving its data-verification system, harmonising international rules and including mining giants Australia, Canada, China, South Africa and Russia in the discussion.

The Transparency Problem. The lack of transparency in the capital-intensive extractive sector can lead to market distortions (tax evasion, fraud, price fixing, underhanded acquisition of mining rights), the politicisation of energy decisions in resource-rich countries, and social disparities. This is because the proceeds from resources often go only to elites. According to some estimates, more than a hundred billion U.S. dollars annually go missing from public funds, leading to corruption and organised crime. Such problems have played a part in triggering conflicts in Sudan, Congo, Angola and Niger. Yet, these problems were long neglected at the global level. The current financial crisis has, however, boosted western governments' will to increase control over the financial markets. Building on government-sponsored British and American actions, global transparency initiatives have gained momentum.

Existing Global Initiatives. The British "Extractive Industries Transparency Initiative" (EITI) was presented at the World Summit for Sustainable Development in 2002, and since 2007 has had a permanent secretariat in Oslo. It gathers industries and countries that voluntarily report on payments, such as those for extraction rights, revenues in the form of taxes, and royalties. Yet, after a decade, EITI is still struggling with efficiency and credibility. The BRICS countries, and the EU Member States remain outside. Only recently the U.S., France, UK and Australia have sought EITI affiliation. Moreover, last year, of the 37 participating governments only 18 actually complied with its standards. At the same time, the lack of sanctions for non-compliance is an incentive for major global companies to participate in EITI, including Arcelor Mittal, Chevron, ExxonMobil, PetroBras, Tata Steel, Qatar Petroleum, and the EU-based Areva, Total, GDF Suez, BG Group, BP, Rio Tinto, ENI, Norsk Hydro, Statoil, RWE, and Royal Dutch Shell. Participation by Polish firms is very limited, with only two, Norway-registered daughter companies of Polish PGNIG and Lotos disclosing data–and these are limited to payments made to the Norwegian government.

By contrast, the American initiative is a domestic regulation with global impact. It was introduced in 2009 as a part of a complex financial regulation, the Dodd–Frank Wall Street Reform and Consumer Protection Act (2010). It obliges all extractive companies listed on American exchanges to report annually on their payments to governments, on a country-by-country and project-by-project basis. The first round of reporting, due in 2014, is linked to the fiscal year, thus more timely compared to EITI. Moreover, the provisions are equipped with sanctions for non-compliance, such as the suspension or revocation of a company's registration. What gives the regulation its global impact is simply the scale of activities of extractive industries on the American exchanges. NYSE, Amex, and NASDAQ together have 36% of the global market. As a result, the provisions apply not only to U.S. companies (i.e., Exxon Mobil, Chevron, ConocoPhillips) but also to non-American giants (i.e., PetroChina, CNOOC, BP, Shell, PetroBras, or Rio Tinto). This could also have a domino effect, whereby companies from unregulated markets registered in the U.S. lobby for the harmonisation of rules elsewhere.

The EU Initiative. The American example and the increasing desire to control the financial market have triggered the move for EU regulation. On 12th June, the European Parliament accepted the wording of the revised Transparency and Accounting Directives. Like the U.s. provisions, these stipulate annual reporting, sanctions for non-compliance and applicability to non-European companies. If duly implemented, the reports available on the EU portal from 2018 onwards would cover companies active on such major stock exchanges as the London SE Group (11.1% of the global, listed extractive sector's value), Deutsche Börse Frankfurt (4.5%), and NYSE Euronet (2.8%). In the EU alone, the regulations would cover almost 3,000 companies, the majority of which, including Russian Gazprom, are listed in Germany and the UK. But the EU is not merely replicating the U.S. system. In many respects, it aspires to be a first-mover in the global transparency-governance system. The provisions give new tools of control to the Member States, with a potential scope of sanctions dependent on national laws, ranging from the publication of information on non-compliance ("naming and shaming"), to financial fines. Moreover, they extend to the large, non-listed companies active on the EU markets and even the logging sector. The directives' broad definition of the term "project" would also limit the room for manoeuvre to hide payments to local governments and entities.

Risks Attached. The EU's approach nevertheless has a number of gaps and weaknesses. First, a lack of clear restrictions on the imposition of sanctions could push companies to seek either clearer or, more likely, laxer jurisdictions in the major unregulated stock exchanges, i.e., TMX Toronto, and TMX Venture (10.7%), Australia ASX (4.6%), Shanghai SE, Johannesburg SE (4.4% share each), and Moscow MICEX (4.1%). Second, in their current formulation, the provisions would empower each Member State to impose severe domestic sanctions on companies without providing, or unifying the tools of each Member State to verify the data provided. Disparities could create uncertainty on the business side, resulting in industry opposition, as in the U.S., where an industry organisation is bringing a lawsuit against the legislation. Third, the current provisions would cover just the tip of the iceberg of problems faced by societies in export countries. They are unlikely to put significant pressure on host governments to improve the "fair share" of spending. The information given will remain ambiguous, as companies are not obliged to disclose details of the projects, such as the size, investments or transportation costs.

Recommendations. For the EU to remain competitive and decrease the relative burden on companies, action is needed to diminish regulatory fragmentation globally. Therefore, the standardisation of the stock-exchange transparency rules should be a subject on the G20 agenda as well as the topic of bilateral meetings between the EU and Australia, Canada, China, South Africa, and Russia as well as front-runner U.S. Second, the new EU provisions could theoretically stimulate market creation by providing a strong regulatory base as well as giving insight into the activities of foreign companies operating in the EU. However, as currently formulated, the measures would increase business uncertainty, and the EU internally should work out clearer mechanisms of data verification through closer cooperation between national tax authorities, foreign ministries, and civil society, both in the EU, and abroad. Third, to encourage change in host countries, the EU would do well to cooperate with NGOs such as EITI and with export countries. It has the biggest potential to influence the situation in countries just starting to exploit resources and which do not have entrenched interests—Cambodia, Papua New Guinea, Sierra Leone, South Sudan, Timor and Uganda.

For Poland, this legislation brings the benefit of EU states pooling their weight and greater accountability of companies operating in Poland and other Member States, including suppliers such as Gazprom. The additional reporting burden on companies and the risk of flight from the Warsaw Stock Exchange will be marginal due to the domestic market structure. Out of 30 listed energy and mining companies, mostly Polish, only a few (PGNiG, KGHM, PKN Orlen, Lotos, ČEZ and MOL) have extractive operations abroad. Still, greater access to information could stimulate Polish companies' activities abroad.