

SEC Adopts Rules Requiring Disclosure of Payments by 'Resource Extraction Issuers'

If you have any questions regarding the matters discussed in this memorandum, please contact the following attorneys or call your regular Skadden contact.

Brian V. Breheny
Washington, D.C.
202.371.7180
brian.breheny@skadden.com

Marc S. Gerber
Washington, D.C.
202.371.7233
marc.gerber@skadden.com

Andrew J. Brady
Washington, D.C.
202.371.7344
andrew.brady@skadden.com

* * *

This memorandum is provided by Skadden, Arps, Slate, Meagher & Flom LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This memorandum is considered advertising under applicable state laws.

1440 New York Avenue, NW,
Washington, D.C. 20005
Telephone: 202.371.7000

Four Times Square, New York, NY 10036
Telephone: 212.735.3000

WWW.SKADDEN.COM

On August 22, 2012, the SEC adopted new rules to implement Section 1504 of the Dodd-Frank Act under which “resource extraction issuers” will be required to disclose payments made to foreign governments and to the United States Federal Government for the purpose of commercial development of oil, natural gas or minerals.

Timing and Next Steps

“Resource extraction issuers” will be required to comply with the new rules for fiscal years ending after September 30, 2013, and must include the disclosure in a new specialized disclosure report (Form SD) filed no later than 150 days after the end of the company’s fiscal year. For calendar year companies, the first Form SD will be due by May 30, 2014. As part of the transition rule, a company’s Form SD for a fiscal year beginning before September 30, 2013 is required to disclose payments only for the period beginning October 1, 2013 through the end of its fiscal year.

Although the deadline for the first Form SD is more than a year away, resource extraction issuers may have a significant amount of work to do in preparation. Companies will have to review and undertake changes to their reporting systems and processes to ensure that the necessary information is collected and reported. In addition, the SEC adopting release notes that companies cannot avoid disclosure under these new rules based on confidentiality requirements under applicable foreign laws or under any existing or future agreements entered into by the company. Accordingly, companies should review whether a violation or breach of any such confidentiality obligations may be asserted by foreign governments or contract counterparties, determine the potential consequences and determine what steps may be taken to address conflicts between the disclosure obligations and any such confidentiality obligations.

Resource Extraction Issuers

The new rules define a “resource extraction issuer” as a company that (i) is required to file annual reports with the SEC and (ii) engages in the commercial development of oil, natural gas or minerals. The rules apply to domestic companies as well as foreign companies (both foreign private issuers and government-owned companies) and smaller reporting companies.

Commercial development of oil, natural gas or minerals includes exploration, extraction, processing and export of oil, natural gas or minerals, or the acquisition of a license for any such activity. The adopting release notes that this definition is not intended to capture activities that are ancillary or preparatory to commercial development, such as manufacturing products or equipment used to extract oil, natural gas or minerals.

Whether a company is a resource extraction issuer is a facts and circumstances analysis, although the adopting release contains additional guidance. For example, “processing” includes activities such as removal of impurities from natural gas after extraction

and prior to transport through a pipeline. Processing also includes crushing raw ore prior to smelting, but does not include refining or smelting. Also, commercial development does not include transporting oil, natural gas or minerals for a purpose other than export.

‘Payments’ to the U.S. Federal Government and ‘Foreign Governments’

A resource extraction issuer is required to disclose any payments made during the fiscal year covered by the Form SD by the company, any subsidiary or any other entity under its control¹ to a foreign government or to the U.S. Federal Government for purposes of the commercial development of oil, natural gas or minerals.

Payment. A “payment” is defined as an amount paid that:

- is made to further the commercial development of oil, natural gas or minerals;
- is “not de minimis” (defined as a payment or a series of related payments that equals or exceeds \$100,000); and
- includes:
 - > taxes (including taxes levied on corporate profits, corporate income and production, but not taxes levied on consumption, personal income taxes or sales taxes);
 - > royalties;
 - > fees (including rental fees, entry fees and concession fees);
 - > production entitlements;
 - > bonuses (including signature, discovery and production bonuses);
 - > dividends (other than dividends paid to a government as a common or ordinary shareholder on the same terms as other shareholders); and
 - > payments for infrastructure improvements.

Payments include in-kind payments, such as paying a government in oil instead of money. Companies will have to determine the monetary value of such in-kind payments, based on cost or, if cost is not determinable, fair market value.

Foreign Government. The final rules define a “foreign government” to include a foreign national government and a foreign subnational government, such as the government of a state, province, county, district, municipality or territory. A foreign government includes a department, agency or instrumentality of a foreign government, as well as a company that is at least majority-owned by a foreign government.

Disclosure

Pursuant to the new rules, resource extraction issuers must disclose the following information in an exhibit to Form SD, formatted using XBRL:

- the type and total amount of such payments made for each project relating to the commercial development of oil, natural gas or minerals;

¹ The determination of whether an entity – for example, a project joint venture – is under the control of a resource extraction issuer will require an analysis of all relevant facts and circumstances.

- the type and total amount of such payments made to each government;
- the total amounts of the payments, by category type;
- the currency used to make the payments;
- the financial period in which the payments were made;
- the business segment of the resource extraction issuer (consistent with reportable segments used for financial reporting purposes) that made the payments;
- the government that received the payments and the country in which the government is located; and
- the project to which the payments relate.

The payments must be reported in either U.S. dollars or the company's reporting currency and the company must disclose the method of currency conversion. Although payments must be disclosed on a project-by-project basis, payments such as corporate income taxes and dividends that are levied at the entity level do not have to be allocated by project and may be reported only at the applicable entity level.