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SEC Reporting & Compliance Alert

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

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New Resource Extraction Payment Disclosures Due September 26, 2024

Securities and Exchange Commission (SEC) reporting companies with fiscal years ending December 31 that engage in the commercial development of oil, natural gas or minerals may be required to file a Form SD with the SEC by September 26, 2024.

Form SD is required to report certain payments made in fiscal year 2023 to foreign governments[1] or to the U.S. federal government[2] for the commercial development of oil, natural gas or minerals. These new requirements, which were adopted in 2020, had a two-year transition period.

Background

The final rules reflect the SEC's third attempt to implement the resource extraction disclosure mandate under the Dodd-Frank Act. The SEC first adopted rules in 2012, which were subsequently vacated by the D.C. federal district court in 2013.

In 2016, the SEC adopted new rules, which were rejected by Congress through a joint resolution pursuant to the Congressional Review Act.

Scope of Issuers

The rules apply to all "resource extraction issuers," which includes all U.S. and foreign issuers (including Canadian companies reporting through the multijurisdictional disclosure system) that:

- are required to file annual reports on Forms 10-K, 20-F or 40-F with the SEC pursuant to Section 13 or 15(d) of the Exchange Act, and
- engage in the commercial development of oil, natural gas or minerals.

The rules define "commercial development of oil, natural gas, or minerals" as exploration, extraction, processing and export of oil, natural gas or minerals, or the acquisition of a license for any such activity. The rules state that the definition is designed to capture only those activities that are directly related to the commercial development of oil, natural gas and minerals, and excludes any activities ancillary or preparatory to such commercial development.

[1] For purposes of the rule, "foreign government" means the national government of a foreign country; any department, agency or instrumentality of the national government, or a company at least majority-owned by the national government of a foreign country; and any subnational governments of a foreign country.

[2] For purposes of the rule, the U.S. federal government does not include any subnational governments within the United States.

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To assist issuers in determining the scope of activities covered by the definition, the adopting release provides detailed guidance on the individual terms within the definition.

The following companies are exempt from the disclosure requirements:

- Emerging growth companies that are not subject to an alternative reporting regime (as discussed below).
- Smaller reporting companies that are not subject to an alternative reporting regime.
- Registered investment companies.

Exemptions

The rules provide conditional exemptions from the disclosure requirements for situations in which a foreign law or a preexisting contract prohibits disclosing the payment information if certain requirements are met.[3] An issuer's reliance on these exemptions would not require preapproval from the SEC. The rules also allow issuers to file an application for exemptive relief on a case-by-case basis.

Any issuer relying on an exemption must still file a Form SD and disclose that it is relying on such an exemption and certain other required information.

Delayed Reporting and Transitional Relief

The rules provide that a resource extraction issuer may delay disclosing payment information related to exploratory activities until the Form SD submitted for the fiscal year immediately following the fiscal year in which the payment was made.

For purposes of this provision, the SEC will consider payments to be related to exploratory activities if they are made as part of the process of:

- identifying areas that may warrant examination,
- examining specific areas that are considered to have prospects of containing oil and gas reserves, or
- conducting a mineral exploration program.

In all cases, exploratory activities for oil, natural gas or minerals are limited to those that commenced prior to the commercial development of those resources.

[3] Conditional exemption based on foreign law requires a legitimate conflict of law and an attempt by the issuer to reconcile the conflict with the foreign jurisdiction. Conditional exemption based on a preexisting contract applies when terms adverse to the final rules are expressly included in writing prior to the effective date of the final rules

In addition, the rules provide transitional relief for recently acquired companies that were not previously subject to the resource extraction disclosure rules or an alternative reporting regime. An issuer's obligation to report payment information for the acquired entity commences with the first full fiscal year immediately following the effective date of the acquisition.

Similarly, issuers that recently completed their initial public offerings (IPOs) in the U.S. will not be required to commence reporting payment information until the first fiscal year immediately following the year in which their IPO registration statement became effective.

Payments Subject to Disclosure

Resource extraction issuers are required to disclose on Form SD payments made to the U.S. federal government or to foreign governments that:

- are made to further the commercial development of oil, natural gas or minerals,
- are not de minimis, and
- include any of the types of payments (including in-kind payments) specified in the rules (*e.g.*, taxes, royalties, fees, production entitlements, bonuses, dividends, payment for infrastructure improvements, and community and social responsibility payments that are required by law or contract).

A payment is defined as "not de minimis" if the payment — either made as a single payment or as a series of related payments — is equal to or greater than $100,000 or its equivalent in the resource extraction issuer's reporting currency.

In addition to reporting its own payments, a resource extraction issuer is also required to disclose payments made by a subsidiary or other entity they control, if those entities' financial information must be consolidated under the accounting principles applicable to the issuer's audited financial statements included in its Exchange Act reports.

Resource extraction issuers are not required to disclose the proportionate amount of the payments made by proportionately consolidated entities or operations.

For joint ventures or arrangements where no single party has control, a resource extraction issuer that is the operator of the venture or arrangement and makes payments to governments for the entire venture or arrangement on behalf of its nonoperator members must report all of the payments.

Nonoperator members of the joint venture or arrangement will not be required to report payments that they make to reimburse the operator for their share of the payments, but they will be required to report payments that they, as resource extraction issuers, make directly to governments.

The payment disclosure must be made on a cash rather than accrual basis and need not be audited.

Project Reporting

The rules require resource extraction issuers to disclose payments made to governments during any fiscal year relating to the commercial development of oil, natural gas or minerals by type and total amount per project.

"Project" is defined using the following three criteria:

1. The type of resource being commercially developed (*e.g.*, oil, natural gas or specific mineral; subcategories are not required).
2. The method of extraction (*e.g.*, whether extracted through the use of a well, an open pit or underground mining).
3. The major subnational political jurisdiction (*e.g.*, the government of a state, province, department, county, district, municipality or territory under a foreign national government) where the commercial development of the resource is taking place.

Commercial development activities using multiple resource types or extraction methods may be treated as a single project if such activities are located in the same major subnational political jurisdiction.

Where a resource being commercially developed could cross the borders between, and generate payment obligations in, multiple major subnational political jurisdictions, the rules require the issuer to treat the activities in each major subnational political jurisdiction as separate projects.

For offshore projects, the identification of the major subnational political jurisdiction where the commercial development of the resource is taking place should include the body of water in which the project is located, using the smallest body of water applicable (*e.g.*, gulf, bay, sea), as well as the nearest major subnational jurisdiction. In addition, if the project is equidistant from two major subnational jurisdictions, the issuer may disclose both such jurisdictions.

The rules allow resource extraction issuers to aggregate by payment type any payments that are made at a level below the major subnational government level (*e.g.*, a county, district or municipality), but the issuer must (i) disclose an aggregate amount for each subnational government payee and (ii) identify each subnational government payee.[4]

Form SD Required Disclosures

For any payment required to be disclosed, the rules require resource extraction issuers to disclose the following information in an exhibit to Form SD:

- The total amounts of payments made for (i) each category of payment type (*e.g.*, taxes, royalties, dividends, etc.), (ii) each category of payment type for each project and (iii) each category of payment type for all projects paid to each government.
- The currency used to make the payments.
- The fiscal year in which the payments were made.
- The business segment of the resource extraction issuer that made the payments.
- The government that received the payments and the country in which each such government is located.
- The project of the resource extraction issuer to which the payments relate.
- The particular resource that is the subject of commercial development.
- The method of extraction used in the project.
- The major subnational political jurisdiction of the project.

Alternative Reporting

The final rules provide a framework for companies to apply for recognition by the SEC of an alternative reporting regime (such as that of the European Union or Canada) that satisfies the transparency objectives of the resource extraction disclosure requirement.

Subject to certain conditions,[5] this framework would permit an issuer to submit an alternative report that was required by an approved foreign jurisdiction in lieu of a separate report that complies with the SEC's disclosure requirements.

[4] In the adopting release, the SEC cites the example of a company with extractive operations in the three oil sands regions of Alberta, Canada (the Regional Municipality of Wood Buffalo, Northern Sunrise County and the Municipality of Cold Lake), for which an issuer would be required to identify each such subnational government entity, as well as aggregate and report all of its fees paid for environmental and other permits to each such entity.

[5] An issuer will only be permitted to use an alternative report for an approved foreign jurisdiction or regime if the issuer was subject to the resource extraction payment disclosure requirements of that jurisdiction or regime and made the report prepared in accordance with that jurisdiction's requirements publicly available prior to submitting it to the SEC.

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The SEC order accompanying the final rule amendments designates the following five resource extraction payment disclosure regimes as alternative reporting regimes that satisfy the required transparency objectives:

- Canada's Extractive Sector Transparency Measures Act.
- EU Accounting Directive 2013/34/EU.
- EU Transparency Directive 2013/50/EU.
- U.K. Reports on Payment to Governments Regulations 2014.
- Norwegian Regulations on Country-by-Country Reporting.

Accordingly, a resource extraction issuer that submits a report complying with the reporting requirement of any of these specified regimes will be deemed to satisfy the requirements under the SEC resource extraction payment disclosure rules.

Anti-Evasion

Any payments not meeting the requirements for disclosure under the rules must still be disclosed on Form SD, if such payments were part of a plan or scheme to evade these disclosure requirements.

Filing Requirements and Liability of Disclosures

The resource extraction disclosures are required on a Form SD and must be tagged using XBRL (eXtensible Business Reporting Language). The Form SD will be deemed "furnished" rather than "filed" with the SEC for securities law liability purposes.

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Additional information about the new requirements is available in the release that the SEC issued when it adopted the rules and in Section 2 of Form SD.

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