January 26, 2011

Ms. Meredith Cross
Director, Division of Corporate Finance
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-4628

Re: Proposed Rules Implementing Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Ms. Cross,

We are pleased to offer this Comment on the Proposed Rules implementing Section 1504 of the Dodd-Frank Act.

EarthRights International (ERI) is a non-governmental organization based in Washington, DC, and Thailand that works with communities and local groups around the globe to address issues of corporate accountability and liability for human rights and environmental harms. ERI has extensive experience working with communities in Burma, Peru, Nigeria and other countries that are affected by extractive projects. A member of Publish What You Pay (PWYP), ERI has a particular interest in government revenue transparency in weak governance zones and zones of conflict. The disclosures under Section 1504 will be crucial for citizens and investors in companies operating in countries like Burma, where we and our partner organizations work in the context of a repressive and secretive military regime – a regime that has been designated by the U.S. Government as a country of primary money laundering concern and whose revenues stem overwhelmingly from the extractive operations of foreign oil, gas, and mining companies.

ERI applauds the Commission for proposals that reflect the plain language of Section 1504, which contemplates expansive coverage of domestic and foreign issuers, mandates project-by-project disclosures, and envisages no categorical exemptions. Our Comment supports aspects of the Proposed Rules and focuses on four issues of special concern to ERI in which the Proposed Rules should be amended or clarified to better accomplish the intent of Congress: 1) types of payments covered; 2) entities covered; 3) definition of control; and 4) treatment of disclosures.

US Office
1612 K Street, NW, Suite 401
Washington, DC 20006
Tel: (202) 466-5188
Fax: (202) 466-5189
Email: infousa@earthrights.org

Southeast Asia Office
PO Box 123
Chiang Mai University
Chiang Mai 50202 Thailand
Tel: (66) 81 531 1256
Email: infoasia@earthrights.org

www.earthrights.org

I. Previous Comments

On December 2, 2010, ERI submitted a Comment ("12/2/10 Comment") recommending:

- Fact-based inquiry into control, and reporting on a proportionate-share basis for all non-consolidated joint ventures
- Coverage of all issuers – domestic and foreign – without categorical exemptions
- Monitoring of Level I ADRs to determine whether it may be necessary to include them in the disclosure requirements in the future, due to anti-competitive effects
- No exemptions for contract confidentiality clauses or conflicting local laws

Although it was submitted well before the deadline, ERI's previous Comment was not posted on the SEC's website before the Proposed Rules were issued and, consequently, may not have been considered by the Commission in drafting the Proposed Rules.[1] The 12/2/10 Comment also provided examples of corporate arrangements that underline the need to cast a wide net when identifying controlled entities, and gave examples of how civil society groups and investors in countries like Burma would use Section 1504 disclosures.

We also wish to draw attention to the December 3, 2010, submission by the Human Rights Foundation of Monland (HURFOM), an ethnic Mon organization based inside Burma and on the Thailand-Burma border that works for the restoration of democracy, human rights, and genuine peace in Burma.[2] In their Comment, HURFOM explained Section 1504's potential to strengthen civil society groups' ability to advocate for accountability and transparency from the Burmese regime. They called for the adoption of measures that would allow investors and Burmese civil society groups to make use of Section 1504 disclosures, such as coverage and disaggregation of in-kind payments, social and economic payments, and security payments; inclusion of downstream activities; and measures to facilitate access to information by local communities.

II. Comments on the Proposed Rules

A. Types of Payments Covered

In answer to Requests for Comment Nos. 12, 21, and 62, we support the Proposed Rules requiring issuers to report both on the royalties they pay to governments, and on the production share revenues that governments and state-owned enterprises receive from extractive enterprises. As explained in detail in the 12/2/10 Comment, governments or companies controlled by them are often joint venture partners or shareholders in extractive projects. In such cases, a significant portion of the revenue they realize from the venture comes not from royalties but from their equity stake in the operation – often known as the production share – or from dividends. This share may be in-kind or in cash, but it operates differently from the equity share that a private operator would enjoy, in that the government partner participates on a preferential basis not

[1] The 12/2/10 Comment is now posted and can be found at http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specializeddisclosures-116.pdf.

[2] HURFOM's Comment can be found at http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specializeddisclosures-96.pdf.

available to private entities.[3] The production share or dividend is a benefit provided to the state by the private operators and should be disclosed, no matter what form it takes, and regardless of whether it is paid to the government as a contractual counterparty or a shareholder.

In answer to Request for Comment No. 14, we support the Commission's proposal to include both in-kind and monetary payments under Section 1504. We are, however, concerned that this inclusive approach does not appear in the text of the proposed regulations and suggest that the Commission incorporate explicit regulatory language rather than leaving it to interpretation.

In answer to Requests for Comment Nos. 20 and 22-24, we are concerned that the Commission proposes to exclude significant payments that accrue to the government from private issuers that are properly considered as part of the "commonly recognized revenue stream." The Commission explicitly notes that it does not propose to include social and community payments or payments to improve infrastructure, even when such payments are part of the issuer's agreements with the host government; more worryingly, the Commission does not even mention payments for the provision of security. These are precisely the payment streams that are often most significant to local groups advocating for equitable returns on resources extracted from their communities.

1. Social and community payments and infrastructure upgrades

Extractive companies often spend millions of dollars each year on projects for communities affected by their operations;[4] they also upgrade and renovate major public infrastructure that they may need to use or is otherwise relevant to their operations. These payments may be contractually required by the host government, or they may simply be initiatives undertaken to facilitate operations or build good-will with the local population. Regardless, they represent an in-kind contribution to the state, as they pay for public goods that the state would otherwise be expected to provide. Moreover, given the frequency with which such payments are associated with extractive projects,[5] it would be hard to argue that social and infrastructure payments are not part of the "commonly recognized revenue stream" of resource extraction.

Several other factors also favor inclusion of social and infrastructure payments. First, as the Commission noted in the Proposed Rules, infrastructure payments are often contractually obligated, and many EITI countries are beginning to report social payments as part of the revenue stream of extractive operations. Ghana has already begun reporting social payments, even to entities on a sub-national level, although neither is currently required by EITI.[6] Moreover, EITI is moving toward inclusion of social payments; the EITI Board has already

[3] *See* 12/2/10 Comment at 3 & nn. 5 & 6.

[4] *See, e.g.,* Jad Mouawad, *Shell to Pay $15.5 Million to Settle Nigerian Case*, N.Y. TIMES, June 8, 2008 (noting claim by Shell to have paid $240 million as "contribution to community development" in the Niger Delta in 2008).

[5] *See, e.g.*, *A stitch in time: How companies manage risks to their reputation*, THE ECONOMIST, Jan. 19, 2008; LawGlen Kelley, Note, *Multilateral Investment Treaties: A Balanced Approach to Multinational Corporations*, 39 COLUM. J. TRANSNAT'L L. 483, 506 (2001)

[6] Dilan Ölcer, *Extracting the Maximum from the EITI* (OECD Development Center, Working Paper No. 276, Feb. 2009), at 20, *available at* http://www.oecd.org/dataoecd/56/60/42342311.pdf. In fact, one reason that social payments are not part of EITI may be that EITI does not require reporting to sub-national government entities, the level at which many such payments are made. Of course, Section 1504 does require sub-national reporting, thereby removing an important barrier to the inclusion of social payments in the reporting regime.

received a report from a Working Group commissioned to study such payments and, at the recommendation of the World Bank and other stakeholders, has signaled a desire to adopt the report's recommendations pending the resolution of a number of technical details.[7]

Second, such payments are often quite substantial and are clearly made "to further the commercial development of oil, natural gas, or minerals," as they either directly relate to necessary facilities or (as the Commission recognized in the Proposed Rules) are part of companies' attempt to secure a favorable operating environment. There is a growing recognition that a crucial component of a stable and profitable resource extraction project is a strong relationship with local communities, who support the presence and operations of the company – the so-called "social license to operate."[8] The benefits accruing to the host government as public services that are provided by private companies should be known to investors so that they may accurately assess the risks of the project.

Third, social and infrastructure payments are often associated with major abuses or are otherwise relevant to the stability of investments, and are therefore of great interest to investors.[9] Perhaps the most glaring example of the link between infrastructure payments, human rights abuses, and instability that is threatening to investments is the case of Talisman Energy in Sudan. Between 1999 and 2001, a consortium including a wholly-owned indirect subsidiary of Talisman Energy assisted in constructing all-weather roads and maintained and upgraded airstrips in a region of Sudan that was convulsed by civil war.[10] Prior to this construction, at least one of the airstrips had been a dirt strip that was not used with frequency by anyone.[11] The Sudanese military, which provided both security and defense against rebel incursions under an agreement with the consortium, was more mobile in difficult weather due to the consortium's roads[12] and was able to stage bombing runs on rebel sites and civilian communities from the consortium's airstrips.[13]

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[7] EITI International Secretariat, Minutes of the 13th Board Meeting (Nov. 11, 2010), at 11, *available at* http://eiti.org/files/121110_Minutes%20of%20the%2013th%20Board%20Meeting.pdf. In fact, several industry representatives of oil companies requested that the Board refrain from acting on social payments until after the outcome of the Section 1504 regulatory process, to avoid conflicting requirements; a representative of the mining industry concurred, suggesting that "it might well be necessary for . . . [social payments] to be dealt with over a longer timescale." Five days later, the National Mining Association submitted a Comment to the Commission advocating exclusion of social payments from Section 1504. *See National Mining Association White Paper on SEC Implementation of Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Extractive Resource Issuer Disclosure of Payments to Governments)* (Nov. 16, 2010), at 3, *available at* http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specialized-disclosures.shtml#comments. If the EITI Board, at the request of industry, is waiting for the Commission to act, and the Commission allows industry objections to derail the inclusion of social payments in Section 1504, then the Commission's action could have the unintended consequence of preventing the evolution of revenue transparency through the EITI process.

[8] *See* Jacqueline L. Nelsen, *Social License to Operate*, 20 INT'L J. MINING, RECLAMATION & ENV'T. 161-62 (2006).

[9] Payments made under the heading of "social payments" have also been used to hide bribery; greater transparency would therefore make it more difficult for companies to hide this form of corruption. *See, e.g.*, Baker Hughes, *Foreign Corrupt Practices Act (FCPA) Compliance Guide* (May 2010), at 16, *available at* http://www.bakerhughes.com/assets/media/assets/4bf2bd3cfa7e1c0cb0000039/file/posted_final_-fcpa-guide_27may2010.pdf.pdf.

[10] *Presbyterian Church of Sudan v. Talisman Energy, Inc.*, 453 F. Supp. 2d 633, 650, 651-53 (S.D.N.Y. 2006).

[11] *Id.* at 653.

[12] *Id.* at 676.

[13] *Id.* at 651-55.

Consortium officials acknowledged that the airstrips were ideal for attacks on certain areas,[14] and that their availability for use by helicopter gunships both had security benefits for the consortium's operations and gave the government the capability to carry out attacks that likely included human rights abuses.[15]

EarthRights International's own experience with the French oil company Total S.A.'s Socio-Economic Program (SEP) in Burma demonstrates that social and infrastructure payments can increase tensions within communities and exacerbate the risk of human rights abuse, and that the way in which such programs are reported can deprive investors of material information. Total has claimed that nearly everyone in their pipeline corridor received benefits from the educational, health, and livelihoods support programs funded by the SEP. Yet ERI's researchers have found that villagers could not afford care at the Total-funded hospital, which in any case offered care inferior to that available at refugee camps on the other side of the border. Villagers complained that the schools supposedly funded by Total refused to allow instruction in their own native language, exacerbating the ethnic repression they already experienced from the Burmese government. Many families found themselves economically worse off after enrolling in Total's micro-credit and agricultural support programs, which were administered in such a way as to actually increase their financial risk.[16] And communities reported that they had to contribute forced labor for Total's infrastructure improvement projects – serious allegations of human rights abuse that could increase Total's exposure to litigation.[17] Transparency would enable communities to understand the payments that directly affect their social structure and to work better with companies to ensure that social benefits accrue more optimally. It would also provide material information to investors in assessing risks associated with their holdings.

2. Security Payments

Security for extractive projects, particularly outside of company compounds, is commonly provided in part or in whole by the host state. Provision of security is not merely preparatory or ancillary to resource extraction; it is a significant and ongoing expense that companies incur from the exploration phase all the way through the lifetime of a project. Payments for security can come in many different forms – they might be ad hoc, mandated by contract, or even by statute. In Nigeria, for example, there have historically been extreme statutory restrictions on the scope of private security firms. Oil companies are obliged to hire supernumerary "SPY" police, who are seconded from public police forces and placed at the disposal of the company.[18] SPY police provide for the companies' everyday security needs; more serious incidents are the

[14] *Id.* at 652.
[15] *Id.* at 653-54.
[16] ERI, TOTAL IMPACT: THE HUMAN RIGHTS, ENVIRONMENTAL, AND FINANCIAL IMPACTS OF TOTAL AND CHEVRON'S YADANA GAS PROJECT IN MILITARY-RULED BURMA (MYANMAR) 47-61 (Sept. 2009). Total reports that the budget for the SEP was over $1 million in 2007. *See* Total, S.A., The Socio-Economic Program: Financial resources, *at* http://birmanie.total.com/en/engagement/p_3_1_3.htm.
[17] ERI, TOTAL IMPACT, *supra* note 16, at 20-25.
[18] *See* RITA ABRAHAMSEN & MICHAEL C. WILLIAMS, SECURITY BEYOND THE STATE: PRIVATE SECURITY IN INTERNATIONAL POLITICS 138 (2011).

purview of the Nigerian armed forces, for whom the oil companies pay transportation, accommodation, and per diem expenses.[19]

There is little question that the depth of an extractive company's financial involvement with host government security forces is of concern and interest to U.S. investors. An ever-increasing number of lawsuits – mostly in the U.S., but also in the courts of several other states – accuse multinational extractive companies of paying security forces for or otherwise being complicit in the commission of gross human rights abuses, including crimes against humanity, war crimes, torture, extrajudicial killing, enforced disappearance, and forced labor.[20] Liability for such acts could reach into the tens of millions of dollars if not higher; in litigation against Royal Dutch Petroleum Co. on which ERI was counsel, for example, the company settled the human rights claims of ten plaintiffs for a total of US$15.5 million dollars. The financial significance of this litigation threat is such that at least one major corporate law firm has recently announced the creation of a practice group dedicated solely to transnational tort defense.[21] Therefore, the payments companies make to states for security should be reported and explicitly designated to better allow investors to assess the material risk to their investments.

B. Entities Covered

In answer to Requests for Comment Nos. 1 and 3, ERI applauds the Commission's proposal to apply the same disclosure requirements to all domestic and foreign issuers, regardless of size or extent of involvement in the industry. ERI does not believe that the required disclosures are unduly burdensome or risk putting disclosing issuers at a competitive, nor have the comments offered by industry participants provided any basis other than generalized conjecture that this might be so. Moreover, in its December 17, 2010 Comment, the Revenue Watch Institute has provided concrete, convincing evidence to the contrary.[22] By the same token, even if Section 1504 disclosures could pose some competitive risk to covered issuers, exempting small businesses or foreign issuers would hardly mitigate that disadvantage. Rather, the way to comply both with the mandate of Congress to require project-by-project disclosures from all issuers and with the SEC's general mandate to mitigate anti-competitive effects is to apply the disclosure requirements as broadly as possible under the statute.

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[19] The Voluntary Principles on Security and Human Rights (VPSHR), a well-regarded voluntary multi-stakeholder initiative that includes states, civil society, and multinational companies, expressly contemplates that companies will be expected to "contribute to, or otherwise reimburse, the costs of protecting Company facilities and personnel borne by public security." It further counsels companies to use all lawful and appropriate means to maintain the control over such personnel's actions necessary to prevent human rights abuses. *See* VPSHR, Interactions Between Companies and Public Security, *at* http://www.voluntaryprinciples.org/principles/public_security.

[20] *See* BETH STEPHENS ET AL., INTERNATIONAL HUMAN RIGHTS LITIGATION IN U.S. COURTS 314-319 (2d ed. 2008) (section on "Indirect Corporate Action"); Robert C. Thompson *et al.*, *Transnational Corporate Accountability for the 21st Century: Translating* Unocal *– The Expanding Web of Liability for Business Entities Implicated in International Crimes*, 40 GEO. WASH. INT'L L. REV. 841, 842 887 (2009).

[21] *See* Amanda Bronstad, *Gibson Dunn Building a Practice Around Transnational Defense*, NAT'L L.J., Jan. 4, 2011, *available at* http://www.law.com/jsp/article.jsp?id=1202476909968.

[22] *See* Peter Rosenblum & Susan Maples, *Contracts Confidential: Ending Secret Deals in the Extractive Industries* (Revenue Watch Institute, 2009), included as attachment to Letter from Karin Lissakers, Executive Director, Revenue Watch Institute to Meredith Cross, Director, Division of Corporate Finance, SEC (Dec. 7, 2010), *at* http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specializeddisclosures-113.pdf.

By way of example, the Foreign Corrupt Practices Act (FCPA) has raised competitiveness concerns similar to those posited by industry representatives on Section 1504. The FCPA, like Section 1504, covers all companies with securities registered under Section 12 of the Exchange Act or that are required to file reports under Section 15(d) of the Exchange Act, including companies that hold ADRs. Yet the response to this concern was not to categorically exempt any class of issuers from the FCPA's requirements. Rather, the broad application of the FCPA protected U.S. business; to further mitigate any possible disadvantage, the executive successfully pursued an international treaty and encouraged U.S. trading partners to pass similar legislation. In addition, Congress eventually passed amendments that *extended* the jurisdictional scope of the FCPA and gave prosecutors greater enforcement powers for extraterritorial bribery.[23]

Moreover, we submit that it would not be in the interests of U.S. investors to exempt smaller businesses from any of the disclosure requirements of Section 1504. Although we recognize that the costs of compliance with new disclosure requirements may have a proportionately higher impact on smaller issuers, a number of factors weigh in favor of including such issuers in the disclosure regime. First, as the Publish What You Pay Coalition noted in their November 22, 2010 Comment to the Commission, U.S. companies are already required to make equivalent disclosures to tax authorities, and it is reasonable to expect that the systems developed for such reporting can be adapted without undue cost.[24] Second, studies have shown that small companies are more prone to inaccurate financial disclosures; because their investors are much more likely to be ordinary – rather than institutional – investors, they are disproportionately affected by information asymmetries and are therefore less able to price securities accurately.[25] In other words, exemption of smaller issuers could disproportionately affect ordinary investors by depriving them of statutorily required information about the companies in which their investments predominate. Such action would have to be justified by convincing evidence that compliance with Section 1504 would be unduly burdensome, rather than mere speculation.

<u>In answer to Request for Comment No. 72</u>, as we suggested in our 12/2/10 Comment, the Commission need not decide at this point whether to extend Section 1504 disclosure requirements to issuers who are exempt from filing requirements pursuant to Exchange Act Rule 12g3-2(b). It should, however require continuous monitoring of the use of Level I ADRs that are exempt from SEC reporting requirements. The Commission could use registration data to compare the usage of the ADR I exemption in future years with that in past years. If more issuers begin registering Level I ADRs and fewer use higher-level ADRs, or if Level II or III ADRs increasingly seek to change their status to Level I – thereby leaving U.S. companies as the primary entities required to disclose their payments under Section 1504 – then the Commission

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[23] *See* Justin Serafini, *Foreign Corrupt Practices Act*, 41 Am. Crim. L. Rev. 721, 722-24. Recently, the U.S. Chamber of Commerce has taken aim at the FCPA, proposing amendments that would curb enforcement authority in various ways. *See* U.S. Chamber Institute for Legal Reform, *Restoring Balance: Proposed Amendments to the Foreign Corrupt Practices Act* (Oct. 2010). The proposals focus on what the Chamber sees as government overreach in enforcing the FCPA, however; there is no suggestion that the coverage of the statute should be narrowed so as not to cover as many issuers.

[24] Publish What You Pay United States, *Comments of Publish What You Pay on Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Nov. 22, 2010), at 17, *available at* http://www.sec.gov/comments/df-title-xv/specialized-disclosures/specializeddisclosures-82.pdf.

[25] *See* John L. Orcutt, *The Case Against Exempting Smaller Companies from Sarbanes-Oxley Section 404: Why Market-Based Solutions Are Likely to Harm Ordinary Investors*, 14 FORDHAM J. CORP. & FIN. L. 325 (2009).

may revisit the issue and decide whether to extend reporting requirements to otherwise exempt issuers pursuant to its authority under Section 12(f)(1)(D) of the Exchange Act.[26]

C. Definition of control

In answer to Requests for Comment Nos. 50 and 51, we applaud the Commission for requiring a fact-based inquiry into control, and defining "control" consistently with the definition under the securities laws. We agree strongly that an issuer may effectively control an entity even if that entity is not a consolidated subsidiary or the operator of a joint venture; the 12/2/10 Comment provides the details of a number of business arrangements that evidence such control. As we explained in greater detail in the 12/2/10 Comment, issuers should be required to report the full measure of payments for all consolidated entities, and to report on a proportionate-share basis for all non-consolidated ventures.

D. Treatment of the disclosures

In answer to Request for Comment Nos. 88 and 89, ERI is alarmed by the Commission's proposed finding that Section 1504 disclosures have a purpose that is distinct from other disclosure regimes, and that therefore they should be treated as "furnished" rather than "filed" for the purposes of private liability under the Exchange Act. We believe that issuers should be required to file Section 1504 disclosures for three reasons: 1) There is no basis for distinguishing Section 1504 from other disclosure requirements, as Section 1504 is primarily intended to protect investors; 2) the rationales given by the Commission for allowing certain other disclosures to be furnished rather than filed do not apply to Section 1504; and 3) the Commission ignores the very real and historically proven temptation for issuers to provide incomplete or misleading information about the payments they make to foreign governments.

1. The purposes of disclosure

The Commission's Proposed Rules note that Section 1504 calls for rules that "support the Federal Government's commitment to international transparency promotion efforts relating to the commercial development of oil, natural gas, or minerals,"[27] and concludes that the nature and primary purpose of Section 1504 is therefore "qualitatively different" from other disclosure regimes. ERI respectfully disagrees with this analysis; although Section 1504 disclosures will of course provide transparency benefits that extend far beyond the U.S. investment community, it is clear that the bill received bipartisan report because its central objective was to protect U.S. investors and improve the investment climate for multinational companies.

As Senator Lugar (R-IN) noted during the Senate debate on the transparency amendment, "Transparency empowers citizens, investors, regulators, and other watchdogs . . . its passage would empower investors to have a more complete view of the value of their holdings." While the Senator did emphasize the desirability of allowing citizens of resource-rich countries to hold

[26] We recognize that the Commission has not, to date, used its authority under Section 12(f)(1)(D) to extend reporting requirements to holders of Level I ADRs, but we submit that such measures could be appropriate if necessary to comply with the mandate of Congress without unduly disadvantaging U.S. businesses.
[27] Proposed Rules at 60.

governments to account for resource revenues, he underlined repeatedly the interests U.S. investors have in transparency, including "increas[ing] the reliability of commodity supplies," clarifying "unique tax and reputational risks," and bringing to light "unstable and high-cost operating environments for multinational companies" whose effects are material to investors.[28]

The Commission's conclusion that Section 1504 disclosures are qualitatively different from standard disclosure requirements that, presumably are deemed to have a traditional investor protection function, appears to be based largely on 15 U.S.C. 78m(q)(2)(E), which reads:

> INTERNATIONAL TRANSPARENCY EFFORTS.—To the extent practicable, the rules issued under subparagraph (A) shall support the commitment of the Federal Government to international transparency promotion efforts relating to the commercial development of oil, natural gas, or minerals.

Yet the very language of this clause indicates that supporting international transparency promotion efforts is *not* the primary purpose of Section 1504. If this were so, the implementing regulations would not support those efforts merely "to the extent practicable," but rather would be specifically directed toward furthering them. It follows that Congress's primary objective in drafting Section 1504 is to protect investors from risks; the implementing regulations will in all cases be required to serve *that* purpose – and not merely "to the extent practicable."

2. Inapplicability of previous rationales for allowing "furnishing" rather than "filing"

The Commission cites three submissions that issuers are required to make, but which are treated as furnished, as precedent for relieving issuers of the obligation to file Section 1504 disclosures. But the exemption of each of these other submissions has a clear statutory basis or reflects concerns about the allocation of authority within the corporate structure – rationales that in no way apply to Section 1504. In short, none of these precedents provides a basis for exempting issuers from liability for misstatements that harm investors, as discussed in detail below.

a. Rule 13a-14(b) and 15d-14(b) certification

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[28] Sen. Richard Lugar, Floor Speech on Transparency Amendment (May 17, 2010), *available at* http://lugar.senate.gov/news/record.cfm?id=325030&. Other Senate supporters made similar observations. *See, e.g.*, Sen. Benjamin Cardin, Floor Speech on Transparency Amendment (May 17, 2010), *available at* http://www.c-spanvideo.org/videoLibrary/clip.php?appid=598156899 ("Investors need to know the full extent of a company's exposure when they are operating in countries where they are subject to expropriation, political and social turmoil, and reputational risks."); Sen. Christopher Dodd, Floor Speech on Transparency Amendment (May 17, 2010), *available at* http://www.c-spanvideo.org/videoLibrary/clip.php?appid=598157015 ("I believe that many Americans – including investors and other stakeholders in these firms – would consider this kind of information material and relevant to their decisions about whether or not to invest, or whether to divest their current holdings, from firms engaged in this sort of activity."). *See also* Calvert Investments, *Calvert Applauds U.S. Congress Passage of Resource Payment Reporting Requirements in the Dodd-Frank Wall Street Reform and Consumer Protection Act* (July 15, 2010), *at* http://www.calvert.com/newsArticle.html?article=16523 (quoting Calvert Senior Vice President Bennett Freeman as saying, "The resource payment disclosures . . . are necessary to evaluate the reputational, regulatory and taxation risks involved in operating in an era in which all the easy to access resources are gone.").

Pursuant to Section 906 of the Sarbanes-Oxley Act (SOX), Rules 13a-14(b) and 15d-14(b) were amended in 2003 to require certification by the CEO or CFO of an issuer that any periodic report complies fully with Sections 13(a) and 15(d) of the Exchange Act. The Commission decided to allow companies to furnish this certification, rather than to file it, because the text of Section 906 requires merely that the certifications "accompany" a periodic report. By contrast, the Commission noted that certifications pursuant to SOX Section 302 were to be "included 'in' the periodic report," and therefore required them to be filed.[29] Section 1504 of the Dodd-Frank Act tracks the language of Section 302 by requiring the issuer to "to include in an annual report" the payment information. Yet despite the fact that exactly such language was a sufficient basis for the Commission to find that Congress intended filing in the case of Section 302, the Commission inexplicably finds it to be a basis for *not* requiring filing in the case of Section 1504.[30] ERI strongly recommends that the Commission interpret its statutory mandate consistently and require that Section 1504 disclosures be filed.

b. Audit Committee Reports

In 1999, Item 407(d) of Regulation S-K was revised, requiring issuers to provide a report on their Audit Committees, including names of directors, information on non-independent directors on the audit committee, the audit committee charter, and certifications on regulatory compliance. The Commission decided to follow the recommendations of a NASDAQ-sponsored blue ribbon committee on corporate audit committees and exempt issuers from private liability for anything contained in the audit report,[31] reflecting the committee's appreciation of "the impracticability of having the audit committee do more than rely upon information it receives, questions, and assesses in making this disclosure."[32]

The Commission's decision to provide a "safe harbor" from liability for audit committee reports reflected its concern that although company directors play a critical role in overseeing financial statements, it would be unfair to hold an issuer liable for its directors' certifications on materials that are ultimately the responsibility of management. The Commission found that this could lead to a confusion of the roles of directorship and management and could inappropriately subject companies to litigation risk. Section 1504 disclosures, on the other hand, do not require any corporate officer to certify anything about any information to which he or she does not have direct access, and filing such disclosures would pose no risk of confusing the roles of directors and managers. Section 1504 does not involve the directorship; it merely requires additional financial disclosures that management is completely qualified to make.

c. Compensation Committee Reports

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[29] SEC, *Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports*, Release No. 33-8238 (June 18, 2003) [68 FR 36636, 36652] (final rule), *available at* http://www.sec.gov/rules/final/33-8238.htm.

[30] Proposed Rules at 59 ("The statutory language of Section 13(q) does not specify that the information about resource extraction payments must be "filed," rather, it states that the information should be 'include[d] in an annual report[.]'") (internal quotations modified).

[31] SEC, *Audit Committee Disclosure*, Release No. 34-41987 (Oct. 14, 1999) [64 FR 55645, 55656] (proposed rule); SEC, *Audit Committee Disclosure*, Release No. 34-42266 (Dec. 30, 1999) [64 FR 73389, 73395] (final rule).

[32] Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committee Reports, *Report and Recommendations* 34-35 (1999), *available at* www.nasdaq.com/about/Blue_Ribbon_Panel.pdf.

In 2006, Item 407(e)(5) of Regulation S-K was revised, requiring issuers to submit a report stating whether the Compensation Committee has reviewed and discussed the "Compensation Discussion and Analysis" required by the regulations, and whether the committee has recommended that such analysis be included in the annual reports. Originally, the Commission proposed for this report to be filed rather than furnished. Under the regulations promulgated a decade earlier, the Compensation Committee Report had been exempted from filing because it was believed that there would be a more robust discussion about compensation procedures if there were no risk of litigation, but the Committee found that the safe harbor provision had not successfully prompted adequate disclosure and recommended that it be abolished.[33] In the Final Rules, however, the Commission agreed to let issuers furnish these reports, responding to concerns that compensation committees would be too preoccupied with the disclosure process and would suffer inappropriate intrusion by management officials who are required to certify incorporated materials.[34]

Neither of the two bases for excluding Compensation Committee Reports from filing requirements applies to Section 1504 disclosures. The concerns that originally prompted exemption in 1992 – that shareholders would inappropriately use compensation policy disclosures to hold issuers civilly liable for policy decisions, and that compensation policy makers would artificially censor their reports in fear of such litigation – have no bearing on revenue transparency, which touches on operational practices (not policies) that entail tremendous financial and reputational risk. And the Commission's basis for retaining this exemption – a concern that corporate managers with certification duties might intrude on the operations of the compensation committee and thereby compromise its independence – does not implicate Section 1504, which mandates disclosures that are completely within the province of management.

3. A record of evasion

The long record of companies' evasive treatment of disclosures relating to extractive industries supports the need for a private right of action with relation to Section 1504. Just this month, Global Witness, an organization concerned with natural resource-related conflicts and corruption, released a report detailing the discrepancies between oil production numbers reported by the Chinese National Petroleum Corporation (CNPC) and the Government of Sudan over the past five years. Rampant under-reporting of production numbers may indicate that the national government has deprived Southern Sudan of hundreds of millions of dollars to which it is entitled under the 2005 Comprehensive Peace Agreement, threatening the fragile peace between

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[33] SEC, *Executive Compensation and Related Party Disclosure*, Release No. 33-8655 (Feb. 8, 2006) [71 FR 6542, 6526] (proposed rule). In fact, the rationale for exempting Compensation Committee Reports from filing requirements in the 1992 rules was a bit more nuanced; the Commission considered the issue to be one of policy rather than of fiduciary duty. In other words, it believed that shareholders who were dissatisfied with compensation procedures and policy should elect new directors rather than filing lawsuits. Burdening issuers with liability for their compensation policy reports would likely have a chilling effect on disclosure that was meant to enable investors to "assess how well directors are representing their interests," SEC, *Executive Compensation Disclosure*, Release No. 33-6962 (Oct. 16, 1992) [57 FR 48125] (final rule).

[34] SEC, *Executive Compensation and Related Person Disclosure*, Release No. 33-8732A (Sept. 8, 2006) [71 FR 53158, 53168] (final rule).

North and South that has allowed for the hydrocarbons industry to flourish.[35] Although this report appears to suggest that it is the government that is under-reporting, the company has offered unconvincing reasons for the discrepancies, raising questions as to the accuracy of its own reporting, as well.

Other examples of material inconsistencies in reporting abound. The Nigerian EITI revealed that international oil companies had reported paying over US$14 million less in 2005 than the Central Bank of Nigeria reported receiving from them.[36] A recent evaluation of the implementation of EITI in Mongolia found that companies consistently underreported payments to local governments, recording such payments as costs rather than contributions to the state.[37] And in Liberia, an EITI audit of tax payments uncovered a fraudulent transaction in which AmLib, a U.S.-controlled mining company, claimed to have made an important tax payment that was not actually received by the Government.[38]

As detailed above, CNPC's obfuscation in Sudan may be hiding the extent to which its operations contribute to political instability. In Liberia, Mongolia, Nigeria, and elsewhere, inaccurate reporting on the part of the companies can mask corruption, financial incapacity, and arbitrariness in fiscal systems. The possibility for such misleading disclosures to harm investors is manifest, and there is no reason for the Commission to shield companies from liability if their material misstatements lead shareholders to underestimate the risk to their investments.

Conclusion

We thank the Commission for this second opportunity to provide information and observations on the promulgation of regulations to give Section 1504 of the Dodd-Frank Act its intended effect. We would welcome the opportunity to expand on this Comment and to provide any further supporting or clarifying information to the extent it is useful to the Commission.

Sincerely,

Jonathan Kaufman
Staff Attorney

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[35] Global Witness, *Crude Calculations* (Jan. 2011), *available at* http://www.globalwitness.org/sites/default/files/110104_Crude%20Calculations.pdf. *See also* Global Witness, *Fueling Mistrust* (Sept. 2009), *available at* http://www.globalwitness.org/sites/default/files/pdfs/v12_final_sudan_fuelling_mistrust_lowres.pdf.
[36] Adeola Yusuf, *NEITI Indicts CBN, NDDC in N790 Billion Oil Audit*. DAILY INDEPENDENT (LAGOS), Mar, 26, 2010, *available at* http://allafrica.com/stories/201003260198.html.
[37] Coffey International Development, *Validation of the Extractive Industries Transparency Initiative in Mongolia*, at 20 (Feb. 2010), *available at* http://www.resourceglobal.co.uk/documents/Mongolia%20Final%20Validation%20Report.pdf.
[38] EITI, *EITI Case Study: Addressing the Roots of Liberia's Conflict through EITI* (2009), *available at* http://eiti.org/files/EITI%20Case%20Study%20-%20Liberia.pdf.

Cc:

Ms. Paula Dubberly
Deputy Director Division of Corporation Finance
Securities and Exchange Commission

Mr. Wayne Carnall
Chief Accountant
Division of Corporation Finance
Securities and Exchange Commission

Mr. Paul Dudek
Chief
Office of International Corporate Finance
Division of Corporation Finance
Securities and Exchange Commission

Ms. Tamara M. Brightwell
Senior Special Counsel to the Director
Division of Corporation Finance
Securities and Exchange Commission

Mr. Roger Schwall
Assistant Director
Division of Corporation Finance
Securities and Exchange Commission

Mr. Elliot B. Staffin
Special Counsel
Office of International Corporate Finance
Securities and Exchange Commission