



Extractive Industries  
Transparency Initiative

# EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

Understanding financial  
statements of state-owned  
enterprises

Guidance on using SOEs'  
financial statements as a  
starting point for public  
disclosures

October 2021

This note has been issued by the EITI International Secretariat to provide guidance to implementing countries on meeting the requirements in the EITI Standard. Readers are advised to refer to the EITI Standard directly, and to contact the International Secretariat to seek further clarification. Contact details can be found at [www.eiti.org](http://www.eiti.org).

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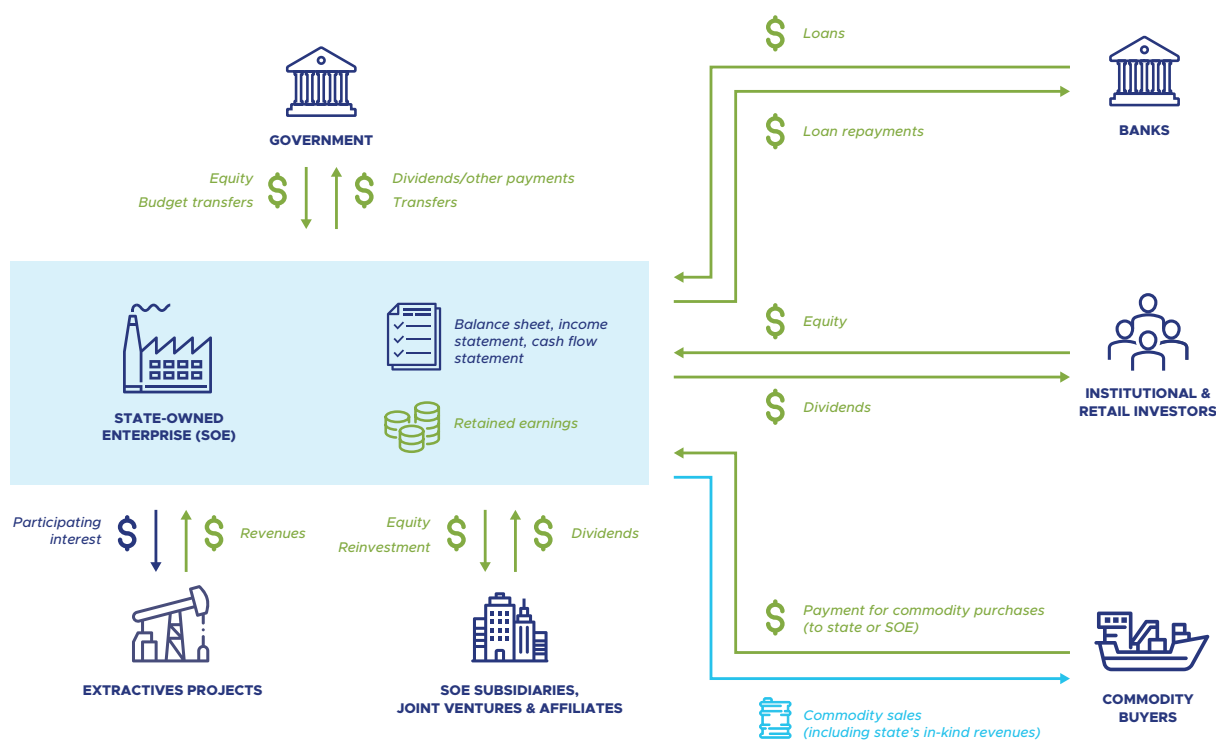
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# Introduction to financial statements

Financial statements provide an overview of the financial performance, financial position and activities of a company in a given period. Companies, including state-owned enterprises (SOEs), usually prepare four main financial statements on a monthly, quarterly and annual basis: the balance sheet, the income statement, the cash flow statement and the statement of shareholders' equity for the period. These statements, along with documents containing significant accounting policies and other explanatory information, describe a company's complete financial position.

## SOE financial relations



The above diagram presents a simplified overview of a state-owned enterprise's (SOE) financial relations with various parties, including the government, SOE subsidiaries, joint ventures and affiliates, the extractive projects in which it participates, SOE lenders and shareholders and business partners such as buyers of its commodities.

In accordance with [Requirement 2.6.b](#) of the EITI Standard, SOEs are expected to publicly disclose their audited financial statements, or the main financial items where financial statements are not available.

These complement the financial disclosures required by the EITI Standard which relate to state participation and SOEs. This note provides guidance to stakeholders, including EITI multi-stakeholder groups (MSGs), on locating information required by the EITI Standard in the standard financial statements of SOEs.<sup>1</sup>

## Key documents

Example Corporation Balance Sheet December 31, 2020	
ASSETS	LIABILITIES
Current assets	Current liabilities
Cash and cash equivalents \$ 2,000	Short-term loans payable \$ 5,000
Receivables 10,000	Current portion of long-term debt 10,000
Accounts receivable - net 10,000	Accounts payable 20,000
Other receivables 1,000	Accrued compensation and benefits 8,000
Inventory 10,000	Income taxes payable 6,000
Supplies 5,000	Other current liabilities 4,000
Prepaid expenses 2,000	Deferred revenues 1,000
Total current assets 38,000	Total current liabilities 51,000
Investments	Long-term liabilities
Property, plant & equipment - net 5,000	Notes payable 20,000
Land 5,000	Bonds payable 100,000
Land improvements 8,000	Deferred mortgage notes 20,000
Buildings 100,000	Total long-term liabilities 140,000
Equipment 200,000	Total liabilities 191,000
Less: accumulated depreciation (80,000)	Common stock 10,000
Property, plant & equipment - net 120,000	Retained earnings 290,000
Intangible assets	Assess other comprehensive income 9,000
Goodwill 100,000	Less: Treasury stock (80,000)
Other intangible assets 10,000	Total shareholders' equity 309,000
Total assets 178,000	Total liabilities & shareholders' equity 309,000

### Balance sheet

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time. It provides a basis for computing rates of return and evaluating its capital structure.

COMPANY B INCOME STATEMENT For Year Ended September 26, 2019 (in thousands)	
NET SALES	\$ 4,958,100
COST OF SALES	2,788,714
GROSS PROFIT	2,169,386
SELLING AND OPERATING EXPENSES	950,430
GENERAL AND ADMINISTRATIVE EXPENSES	293,728
TOTAL OPERATING EXPENSES	1,244,158
OPERATING INCOME	925,228
OTHER INCOME	900
GAIN/LOSS ON FINANCIAL INSTRUMENTS	5,513
EXCHANGE GAIN/LOSS ON FOREIGN CURRENCY	(12,446)
INTEREST INCOME	(14,171)
INCOME BEFORE TAXES	904,124
INCOME TAX EXPENSE	257,642
NET INCOME	\$ 646,482

### Income statement (also called “profit and loss (P&L) statement”)

An income statement is a financial statement that shows the company's income and expenditures. It also shows whether a company is making a profit or loss for a given period. Along with balance sheet and cash flow statement, the income statement gives an indication of a company's financial health.

FY Ended 31 Dec 2017 All figures in USD	
Cash Flow From Operations	
Net Earnings	2,000,000
Additions to Cash	
Depreciations	10,000
Decrease in Accounts Receivable	15,000
Increase in Accounts Payable	15,000
Increase in Taxes Payable	2,000
Subscriptions From Cash	
Increase in Inventory	(30,000)
Net Cash From Operations	2,012,000
Cash Flow From Investing	
Equipment	(500,000)
Cash Flow From Financing	
Notes Payable	10,000
Cash Flow for FY Ended 31 Dec 2017	1,522,000

### Cash flow statement

A cash flow statement is a financial statement that summarises the amount of cash and cash equivalents entering and leaving a company. The cash flow statement measures how a company manages its cash position, meaning how the company generates cash to pay its debt obligations and fund its operating expenses.

FY Ended 31 Dec 2017 All figures in USD	
Net Earnings	2,000,000
Additions to Cash	
Depreciations	10,000
Decrease in Accounts Receivable	15,000
Increase in Accounts Payable	15,000
Increase in Taxes Payable	2,000
Subscriptions From Cash	
Increase in Inventory	(30,000)
Net Cash From Operations	2,012,000
Cash Flow From Investing	
Equipment	(500,000)
Cash Flow From Financing	
Notes Payable	10,000
Cash Flow for FY Ended 31 Dec 2017	1,522,000

### Statement of shareholders' equity

A statement of shareholders' equity indicates changes in the value of shareholders' equity or ownership interest in a company over the course of the accounting period. It gives investors more transparency about the changes in equity accounts and business activities that contribute to changes in the value of shareholders' equity.

1 The guidance provided in this note is based on the assumption that SOE financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) issued by the IFRS Foundation and the International Accounting Standards Board (IASB). These aim to set internationally recognised accounting specifications and policies. See IFRS (n.d.), “List of IFRS Standards and IFRIC Interpretations”, <https://www.ifrs.org/issued-standards/list-of-standards/>.

Financial audits are conducted to obtain an independent opinion of whether a company's financial statements provide a "true and fair" representation of a company's financial performance. In most countries, audits of financial statements are mandatory in order to provide tax authorities and governments assurances that companies adequately calculate their tax base and payments. Financial audits also provide investors with assurances that the financial data is sufficiently reliable to adequately calculate risks associated with investing in the company.

### What can the data help answer?

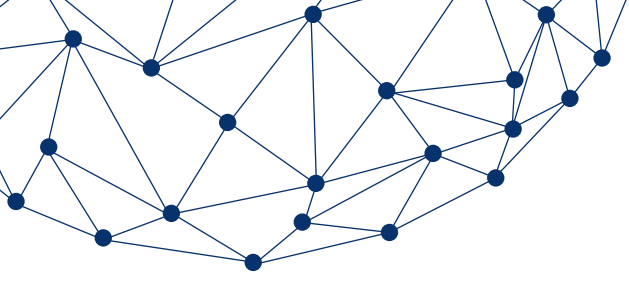
- 1) Is the company in a better financial position at the end of the reporting period than it was at the beginning of the year?
- 2) What resources does the company have?
- 3) How did the company use its cash during the reporting period?
- 4) What return on investment is the company achieving on an annual basis?
- 5) What are the financial risks associated with the company's business?

### Examples of red flags for potential risks to financial health when reviewing financial statements

- **Rising debt-to-equity ratio:** This can indicate that the company is taking on more debt than it can handle. A debt-to-equity ratio that is over 100% is a red flag. It is also recommended to review the falling interest coverage ratio, which is calculated by dividing net interest payments by operating earnings. If the ratio is below five, this can be cause for concern.
- **Several years of revenue trending downwards:** If a company has three or more years of declining revenues, it is questionable whether it will provide a return on investment.
- **Large expenses categorised as "other" on the balance sheet:** Many organisations have "other expenses" that are inconsistent or too small to quantify, a category that is commonly seen on income statements and balance sheets. However, if these "other" line items have high values, it is important to understand their nature and whether they are likely to reoccur.
- **Unsteady cash flow:** Cash flow is a sign of a healthy organisation, although cash reserves should usually fluctuate with the flow of cash. High cash stockpiles can indicate that accounts are being settled, and/or that there is not a large amount of new work. On the other hand, cash shortages can indicate under-billing for work by the company.

- **Rising accounts receivable or inventory in relation to sales:** Capital that is tied up in accounts receivable or has already been used to produce inventory represents funds that cannot generate a return on investment. While sufficient inventory to fulfil orders is important, a company should not hold a significant share of its revenues left as unsold inventory in a warehouse. Significant bad debt provisions indicate that the company is failing to recover a large share of its receivables, which will have an impact on cash flow.
- **Consistently higher liabilities than assets:** Some companies experience a steady stream of assets and liabilities as their business does not depend on seasonal shifts or is less affected by market pressures. However, for businesses that are more cyclical in nature (i.e. construction companies during the winter months), a company's liabilities could outweigh its assets at a given time. Companies can plan for this to reduce the mismatch between assets and liabilities at any given time. However, if a company is consistently assuming more liability without a proportionate increase in assets, it could be a sign that the company is over-leveraged. In some cases, specific liabilities – such as unpaid cash calls or significant penalties and interest payable on delayed settlement of liabilities – could be an indicator of internal challenges within the company. Disclosures of contingent liabilities can indicate potential future liabilities for the company, such as significant unconcluded legal suits against the company. Numerous potential liabilities are a negative indicator.
- **Declining gross profit margin:** The gross profit margin measures a company's ratio of profits earned to costs over a set time period. The profit margin must account not only for the costs to produce the product or service, but the additional funds required to cover operating expenses, such as cost of debt financing. A declining profit margin can be a red flag.

Other examples of red flags can include consistently small margins, low levels of reinvestment, large amounts of short-term debt, lower rates of return and pending lawsuits.



# Overview of EITI

## Requirements related to state participation

### EITI Requirement 2.6

#### State participation

The objective of [EITI Requirement 2.6](#) is to ensure an effective mechanism for transparency and accountability for well-governed SOEs and state participation more broadly through a public understanding of whether SOEs' management is undertaken in accordance with the relevant regulatory framework. This information provides the basis for continuous improvements in the SOE's contribution to the national economy, whether financially, economically or socially.

The requirement covers:

- Publication of SOE audited financial statements (p. 10)
- The rules and practices governing SOEs' financial relations with the state (p. 12)
- State and SOE ownership in the extractive industries (p. 27)
- State and SOE loans and guarantees (p. 31)
- SOE expenditures (p. 34)
- SOE procurement and sub-contracting (p. 36)
- SOE corporate governance (p. 38)

### EITI Requirement 4.2

#### Sale of the state's share of production or other revenues collected in kind

The objective of [EITI Requirement 4.2](#) is to ensure transparency in the sale of in-kind revenues of minerals, oil and gas to allow the public to assess whether the sales values correspond to market values and ensure the traceability of the proceeds from the sale of those commodities to the national Treasury.

The requirement covers in-kind revenues, proceeds of sales and transfers to the state (p. 41), the buyer selection process (p. 47) and sales agreements (p. 48).



## **EITI Requirement 4.5**

### **Transactions related to SOEs**

The objective of this [EITI Requirement 4.5](#) is to ensure the traceability of payments and transfers involving SOEs and strengthen public understanding of whether revenues accruable to the state are effectively transferred to the state and of the level of state financial support for SOEs.

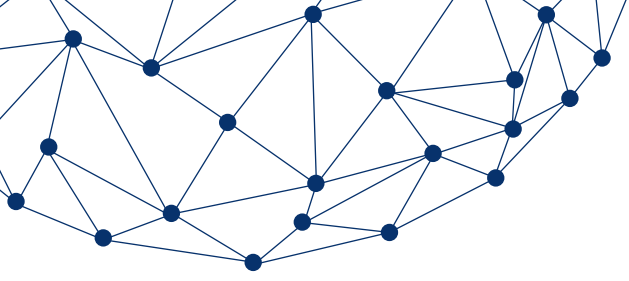
The requirement covers company payments to SOEs (p. 50), SOE transfers to government (p. 51) and government transfers to SOEs (p. 52).

## **EITI Requirement 6.2**

### **SOE quasi-fiscal expenditures**

The objective of [EITI Requirement 6.2](#) is that, where state-owned enterprises undertake extractive-funded expenditures on behalf of the government that are not reflected in the national budget, these are disclosed to ensure accountability in their management.

The requirement covers SOE quasi-fiscal expenditures including social services (p. 53), public infrastructure (p. 54), subsidies (p. 55) and national debt servicing (p. 56).



# Requirement 2.6: State participation

## 1. Publication of SOE audited financial statements

### **EITI Requirement 2.6.b**

#### **Public disclosure of SOE(s)'s financial statements**

In accordance with the EITI Standard, “SOEs are expected to publicly disclose their audited financial statements, or the main financial items (i.e. balance sheet, profit/loss statement, cash flows) where financial statements are not available.”

The main items of a company's financial statements are the following:

- Balance sheet as at the end of the period
- Income statement (also called “profit and loss statement”) for the period
- Cash flow statement for the period
- Statement of changes in equity for the period
- Notes (narrative section) to the financial statements

### **Where to find information**

Financial statements of SOEs, where publicly disclosed, are usually accessible from the SOE's corporate website, the website of the government ministry with jurisdiction over the SOE, or, in certain cases, the public corporate register website. In cases where SOEs' financial statements are audited by the government's national audit office, the audited financial statements can be an attachment to the audit report published on the audit office's website.

**EXAMPLES****SOE websites**

Some SOEs published the audited consolidated financial statements in full on their websites, including [GNPC](#) (Ghana), [NNPC](#) (Nigeria), [Sonangol](#) (Angola), [Naftogaz](#) (Ukraine) and [KazMunayGas](#) (Kazakhstan).

**Government websites**

Some SOEs' audited consolidated financial statements are published on the website of the Ministry of Finance, including SNPC on the [MoF website](#) (Republic of Congo), GNPC's 2011-2013 financial statements on the [MoF website](#) (Ghana).

**Public corporate registers**

Some SOEs' audited consolidated financial statements are published on the public corporate register website, such as Albpetrol on the [QKB National Business Center website](#) (Albania).

**Gaps with EITI disclosure requirements**

Some SOE websites or SOE annual reports publish only a summary of the consolidated financial statements rather than the comprehensive document. In some cases, while the consolidated financial statements may be published in full, the related auditor report may not be disclosed. Some published financial statements may also not be up to date and/or may not have been audited.

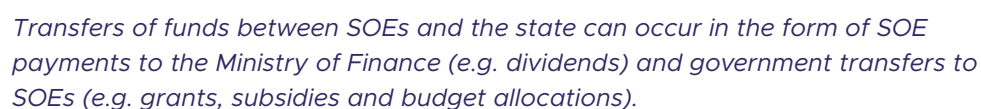
**How the EITI can add value**

The EITI can provide a platform for publication of consolidated financial statements in cases where SOEs do not operate their own websites or face other barriers to disclosure. In some cases, like in Afghanistan in 2018-2019, the EITI provided the impetus for establishing and auditing for the first time the financial statements of the two extractive SOEs.

The EITI can play a role in collating financial statements of SOEs (and indeed other extractive companies) and could lead the development of publicly-accessible database of audited financial statements in cases where such a database is not already in existence.

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## Transfers of funds between the SOE(s) and the state



In accordance with the EITI Standard, “implementing countries must disclose (...) an explanation of the role of state-owned enterprises (SOEs) in the sector and prevailing rules and practices regarding the financial relationship between the government and SOEs, i.e. the rules and practices governing **transfers of funds between the SOE(s) and the state**, retained earnings, reinvestment and third-party financing.”

## Rules related to transfers between SOE(s) and the state

### Where to find information

The rules related to SOEs' distribution of profits, in the form of dividends or other ad hoc transfers to government entities, are not usually described in the SOE's audited financial statement. The rules related to SOEs' entitlement to financial transfers from the government, in the form of budget transfers, subsidies or other forms of financial support, are also not usually described in the SOE's audited financial statement.

Rather, these rules are usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE's statutes or articles of incorporation (sometimes called memorandum of incorporation). In other cases, these financial relations can be codified in the country's Public Finance Management Act.

### EXAMPLES

#### GNPC (Ghana)

According to Article 21 the [1983 GNPC Act](#) (PNDCL 64), GNPC is required to make payments into the Consolidated Fund of any surpluses after taxes and contribution to GNPC's reserve fund.

#### North Coal Enterprise (Afghanistan)

Article 26 of the [2005 SOC Law](#) states that SOEs are entitled to receive funding from the government's development budget.

#### Naftogaz (Ukraine)

Ukraine's Law "[On the Management of State Property Objects](#)" No. 185-16 (21 September 2006) requires SOEs to transfer their dividends directly to the government treasury, to be recorded in the national budget. Although the government has considered that this covers all SOE subsidiaries, the subsidiaries of the SOE Naftogaz claim that they are not covered by this requirement given that they do not meet the definition of SOE under Ukrainian law, which covers only companies that are directly majority-owned by the government, not companies majority owned by SOEs.

## Practices related to transfers between SOE(s) and the state

### Where to find information

Information on transfers from the government to the SOE are usually disclosed as part of the Cash Flow Statement, under "Financing Activities". These transfers to SOEs can be categorised as government "grants", "assistance" or "other income from the state", among other labels.

Information on SOE transfers to the government, including dividends to the state, are usually disclosed as part of the SOE's balance sheet, in the section related to

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

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shareholder equity. Transfers of net profits from the SOE to the state are usually categorised as “distribution of profits” or “statement of stockholders' equity as a subtraction from retained earnings”, among other labels.

As government holds interests in SOEs, the IFRS Standards (IAS 24) require additional details in financial reports on “related party” disclosures, transactions or amounts due/owed. These encompass transactions in both directions (i.e. to and from SOEs) and relate to both cash flows and liabilities. The materiality figures under related party disclosures can be an indicator of the performance of the SOE in terms of transfers to and from the state.

### EXAMPLES

#### **Qatar Petroleum (Qatar)**

The summary of 2018 consolidated financial statements included in [QP's 2018 Annual Review](#) provides the value of dividends transferred by QP to the Ministry of Finance (pp. 78-79), other charges related to the Ministry of Finance (p. 80) and cash transfers to the Ministry of Finance (p. 81). These figures are presented on an accrual basis of accounting.

#### **Pemex (Mexico)**

The “Financing Activities” in Pemex's [2014 consolidated financial statements](#) (pp. 7 and 102) presents the value of financial transfers from the Federal Government of Mexico to Pemex, categorised as “Increase in equity due to Mexican Government contributions”. These figures are presented on an accrual basis of accounting.

#### **SNPC (Republic of Congo)**

Note 34 “SNPC: fiche de synthèse des principaux indicateurs financiers” of SNPC's [2018 financial statements](#) (p. 53) presents the value of dividends declared based on the 2017 and 2018 financial results. These figures are presented on an accrual basis of accounting. In cash-accounting terms, SNPC did not pay any dividend to its sole shareholder (the state) in either 2017 or 2018.

### **Gaps with EITI disclosure requirements**

Not all companies and SOEs record the detailed components of operating income, so some report data on “operational costs”, which also include non-tax transfers to government. SOEs sometimes do not report dividend payments, which could mean that they either did not pay dividends or that dividends were subsumed under other line items in the financial report.

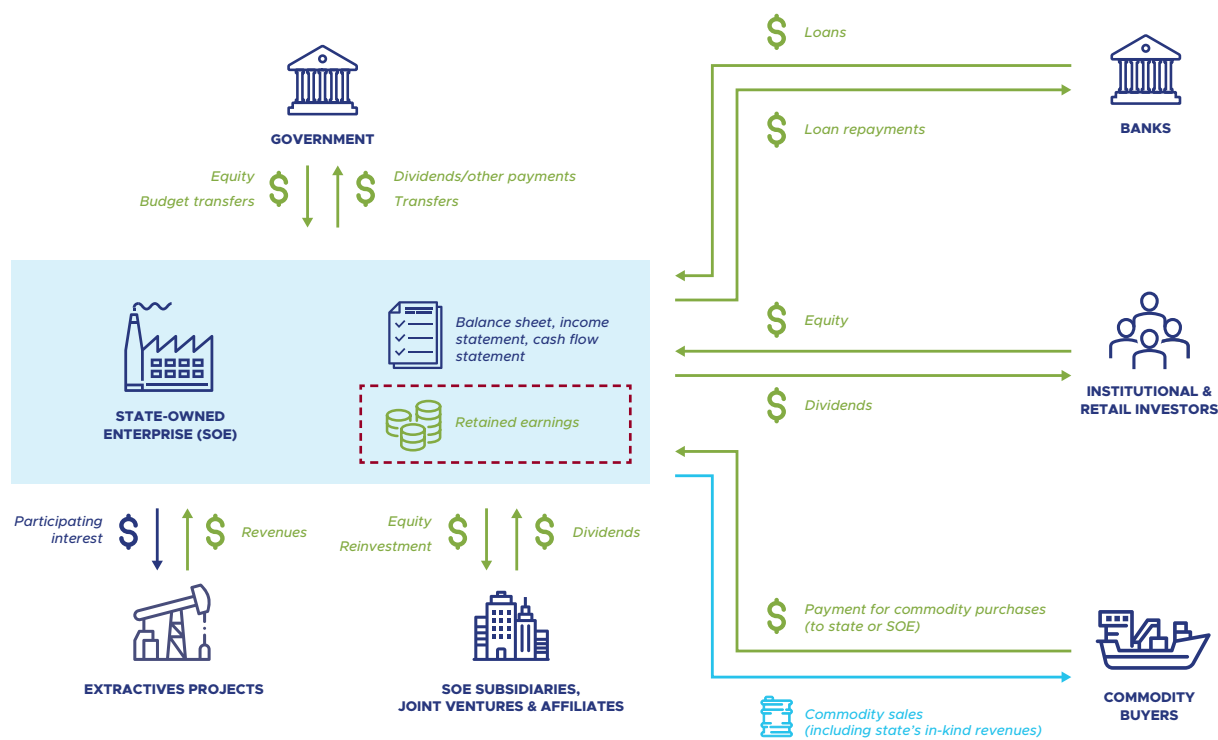
Figures for SOE dividends differ between data presented on an accrual basis of accounting (dividends related to profit recorded for that year) and data on a cash basis of accounting (dividends paid in that year, usually related to profits recorded in a previous year).

## How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of whether the practice of financial transfers between the state and SOEs is in accordance with the statutory procedures.
- Compare cash and accrual accountings of SOEs' transfers to the state, to track both the decisions on dividends and their actual transfers to government, which can strengthen public oversight of SOEs' contributions to government revenues over several years.
- Provide a platform for analysis of SOE payments to government with a view to assess return on shareholder equity, so as to support public debate and policy-making related to oil, gas and mining SOEs.

## SOEs' retained earnings



SOEs' retained earnings consist of all remaining profits after dividends have been distributed to the SOE's shareholders.

## EITI Requirement 2.6.a.i

### Rules and practices governing SOEs' retained earnings

In accordance with the EITI Standard, *“implementing countries must disclose (...) an explanation of the role of state-owned enterprises (SOEs) in the sector and prevailing rules and practices regarding the financial relationship between the government and SOEs, i.e. the rules and practices governing transfers of funds between the SOE(s) and the state, **retained earnings**, reinvestment and third-party financing.”*

The term “retained earnings” in EITI Requirement 2.6.a.i refers to all remaining profits once dividends have been distributed to shareholders. These are usually categorised as “retained earnings”, “net earnings after dividends” or “appropriated/unappropriated retained earnings”, among other labels. Retained earnings cover both the profits that are retained for reinvestment in the company's operations (including both operational and capital expenditures) as well as the profits that are retained for the company's capital reserves or other accounts.

Retained earnings are calculated as follows:

*Retained Earnings (RE) = Period Start RE + Net Income/Loss – Cash Dividends – Stock Dividends.*

## Rules related to SOEs' retained earnings

### Where to find information

The rules related to SOEs' ability to retain earnings are not usually described in the SOE's audited financial statement. Rather, these rules are usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE's statutes or memorandum of incorporation.

### EXAMPLES

#### North Coal Enterprise (Afghanistan)

Article 23 of the [2005 SOC Law](#) requires SOEs to transfer 75% of their net profit to the Ministry of Finance, with the remaining 25% earmarked to different special-purpose funds managed by the SOE.

#### GNPC (Ghana)

According to Article 21 the [1983 GNPC Act](#) (PNDCL 64), GNPC is not allowed to retain earnings from its transfers of profits to the Consolidated Fund.



## Practices related to SOEs' retained earnings

### Where to find information

Information on SOEs' retained earnings are usually disclosed as part of the balance sheet, in the section on equity. The notes to the financial statements provide additional information related to SOEs' retained earnings, as disclosed in the equity section of the balance sheet.

#### EXAMPLE

### Pertamina (Indonesia)

Note 26 "Retained earnings and interim dividend" and "Equity" of PT Pertamina's [2019 consolidated financial statements](#) (pp. 3 and 107) present the value of the SOE's retained earnings, disaggregated between appropriated and unappropriated retained earnings. This information is provided for retained earnings related to the 2017 financial performance (agreed in May 2018) and to the 2018 financial performance (agreed in May 2019). This data is presented on an accrual basis of accounting.

### Gaps with EITI disclosure requirements

Consolidated financial statements by their nature consolidate intra-group transactions at the company level, which means that details of retained earnings by each of the subsidiaries, joint ventures and affiliates in which the SOE holds an equity interest may not be presented in a disaggregated manner. At a minimum, the EITI Standard requires public disclosure of SOEs' retained earnings at a consolidated group level and for any SOE subsidiaries considered material SOEs in their own right.

### How the EITI can add value

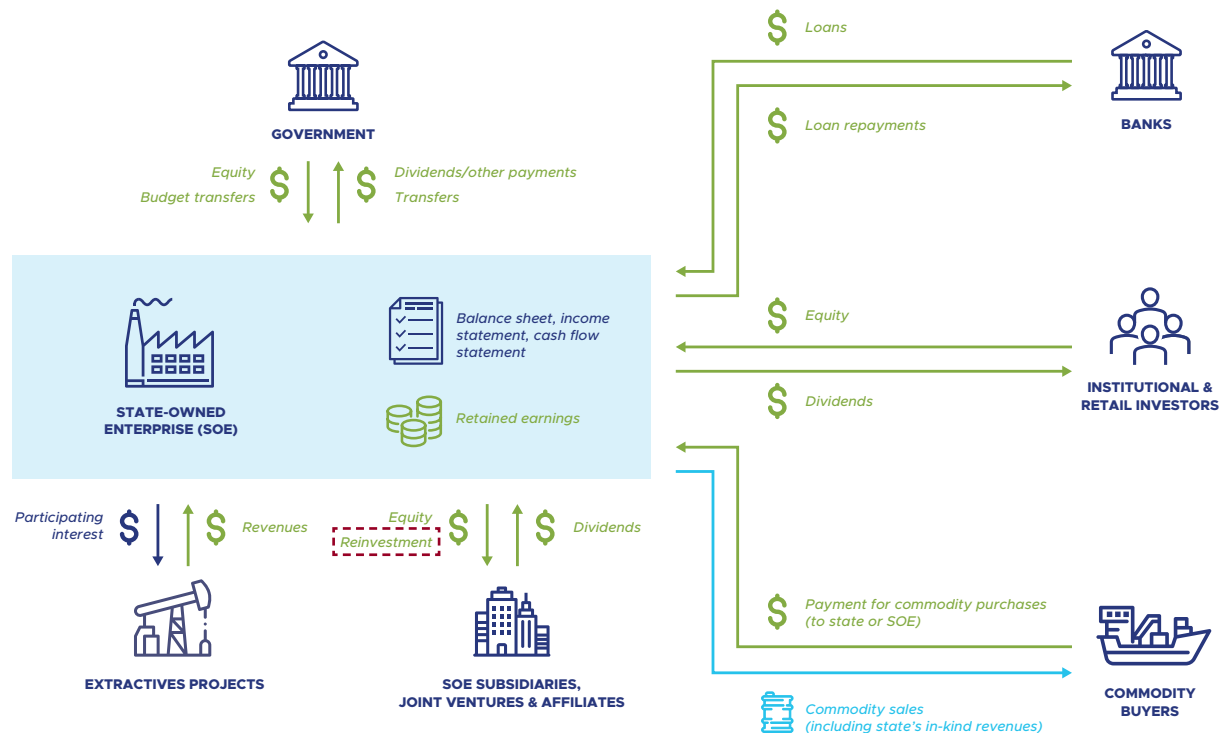
EITI reporting can:

- Track trends in retained earnings and provide a platform for analysis of SOEs' management and allocation of their retained earnings, particularly to ascertain whether the SOEs' distribution of retained earnings is in line with the legal framework and explanations for any variances.
- Compare cash and accrual accountings of SOEs' retained earnings, which can strengthen public understanding of SOEs' financial management over several years.

## EITI REQUIREMENT 2.4

Contracts  
Guidance Note

### SOE(s)' reinvestments



Reinvestments occur when retained earnings are reinvested in the operations of an SOE's subsidiaries, affiliates, joint ventures or the group itself.

### EITI Requirement 2.6.a.i

#### Rules and practices governing SOEs' reinvestment

In accordance with the EITI Standard, “implementing countries must disclose (...) an explanation of the role of state-owned enterprises (SOEs) in the sector and prevailing rules and practices regarding the financial relationship between the government and SOEs, i.e. the rules and practices governing transfers of funds between the SOE(s) and the state, retained earnings, **reinvestment** and third-party financing.”

The term “reinvestment” in EITI Requirement 2.6.a.i refers to all remaining retained earnings that have been reinvested in the operations of subsidiaries, affiliates, joint ventures or the group itself. This is distinct from the retained earnings that an SOE may transfer to its paid-up capital or other types of capital reserves, bank accounts, other accounts, etc. The term “reinvestment” can cover both allocations of retained earnings for operating or capital expenditures.

## Rules governing SOEs' reinvestment

### Where to find information

The rules related to SOEs' ability to reinvest their retained earnings are not usually described in the SOE's audited financial statement. Rather, these rules are usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE's statutes or memorandum of incorporation.

#### EXAMPLE

### NNPC (Nigeria)

Article 9 of the 1977 NNPC Act in the DPR's [Compendium of Oil and Gas Laws and Regulations](#) (pp. 66-77) allows NNPC to reinvest its retained earnings (or to maintain a general reserve) after the direction by the National Council of Ministers for the disposal of any surplus funds.

## Practices related to SOEs' reinvestments

### Where to find information

Information on SOEs' reinvestments is usually disclosed as part of the balance sheet, in the section on assets. More information can be found in the narrative disclosures in the notes to the financial statements, including in the section of notes on property, plant and equipment.

In addition, in the cash flow statement, the value of capital expenditures is reported under the "cash flow from investing" section. The rate of the SOE's reinvestments can be calculated by dividing the company's capital expenditures by the net income.

#### EXAMPLES

### GNPC (Ghana)

Note 19 "Investments in subsidiaries" to GNPC's [2018 consolidated financial statements](#) (pp. 49-52) provides information on the value of GNPC's investment in each of its subsidiaries in the year under review. These figures are presented on an accrual basis.

### NNPC (Nigeria)

Note 6 "Interest in joint operations, associates and joint ventures" and Note 6.3 "Investment in associate" of NNPC's [2019 consolidated financial statements](#) present information on the value of NNPC's investments in its subsidiaries, joint ventures and associates (pp. 16, 51-52, 56). This information includes both cumulative investments as well as new investments in the year under review. The figures are presented on an accrual basis of accounting.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

Understanding financial statements of state-owned enterprises

Guidance on using SOEs' financial statements as a starting point for public disclosures

### Gaps with EITI disclosure requirements

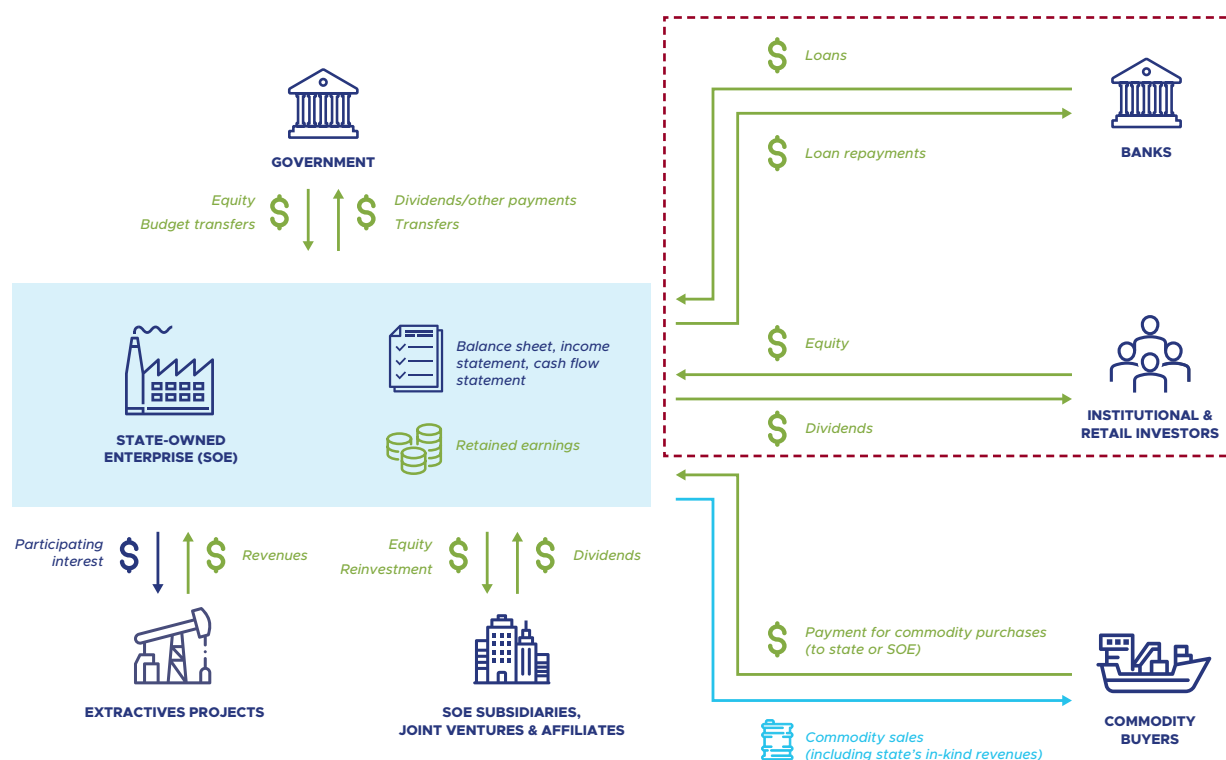
Consolidated financial statements consolidate a company's transactions at the group level. As such, the details of reinvestments in each of the subsidiaries, joint ventures and affiliates in which the SOE holds an equity interest may not be presented in a disaggregated manner. This information can be covered under financial disclosure in accordance with IFRS 12, which requires disclosures on interests in subsidiaries, joint ventures, joint arrangements etc. At a minimum, the EITI Standard requires public disclosure of SOEs' reinvestments at a consolidated group level.

### How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of SOE reinvestments with a focus on analysis of return on investment of SOEs' reinvestments.
- Compare cash and accrual accountings of SOEs' reinvestments, which can strengthen public understanding of SOEs' financial management over several years.

### SOE(s)' third-party financing



*Third-party financing refers to any type of equity or debt financing for the SOE's operations (or those of its subsidiaries, affiliates, joint ventures) that is sourced from entities other than the SOEs' shareholders or the SOE itself (including subsidiaries, affiliates, joint ventures). Third-party financing is often derived from banks, institutional investors or retail investors.*

**EITI Requirement 2.6.a.i****Rules and practices governing third-party financing**

In accordance with the EITI Standard, *“implementing countries must disclose (...) an explanation of the role of state-owned enterprises (SOEs) in the sector and prevailing rules and practices regarding the financial relationship between the government and SOEs, i.e. the rules and practices governing transfers of funds between the SOE(s) and the state, retained earnings, reinvestment and **third-party financing**.”*

The term “third-party financing” in EITI Requirement 2.6.a.i refers to any type of equity or debt financing for the company’s operations (or those of its subsidiaries, affiliates, joint ventures) that is sourced from entities other than the company’s shareholders or the company itself (including subsidiaries, affiliates, joint ventures). Equity finance is a method of raising fresh capital by selling shares of the company to retail or institutional investors. The practice of a company borrowing money to be paid back at a future date (usually with interest) is known as debt financing.

**Rules governing SOEs’ third-party financing****Where to find information**

The rules related to SOEs’ ability to raise third-party financing (either debt or equity) are not usually described in the SOE’s audited financial statement. Rather, these rules are usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE’s statutes or memorandum of incorporation.

**EXAMPLES****Pemex (Mexico)**

Article 106 of the [2014 Petróleos Mexicanos \(Pemex\) Law](#) codifies the rules regarding Pemex’s ability to raise third-party financing (both debt and equity). Based on those rules, the debt limits for Pemex and its subsidiaries are set annually by Congress and published in the annual government budget (Federal Income Law). These debt limits are described in the notes related to debt in Pemex’s consolidated financial statements, for example in Note 16 of Pemex’s [2019 consolidated financial statements](#) (p. 79).

**SNPC (Republic of Congo)**

Article 6 of SNPC’s [2017 company statutes](#) confirm that the company’s equity can only be increased by its sole shareholder (the state), which implies that SNPC is not entitled to raise equity financing from third parties other than the state.

## Practices related to SOEs' third-party financing

### Where to find information

Information on an SOE's third-party debt financing is usually disclosed as part of the balance sheet, in the section on financial liabilities (current and/or non-current). Relevant information may also be found in the cash flow statement, in the section on cash flow from financing activities, with additional information in the notes to the financial statements. These types of third-party debt financings are usually categorised as "short-term loan", "long-term loan", "line of credit", "bond" or "Eurobond", among other labels.

Information on an SOE's equity is usually disclosed as part of the balance sheet, in the section on "total liabilities and stockholders' equity" or "total liabilities and owner's equity". When a company issues equity, the capital raised appears on the cash flow statement (in the section on financial liabilities). The balance sheet reflects both the cash raised and the equity issued. However, equity issuance does not affect the income statement.

### EXAMPLES

#### GNPC (Ghana)

Note 30 "Medium-term loans" to GNPC's [2018 consolidated financial statements](#) (pp. 57-58) provides information on medium-term loans to GNPC and its subsidiaries. For some loans, this includes the value of the loan, the interest rate, tenor and repayment modalities. However, this information is not consistently provided for all loans to GNPC and its subsidiaries.

#### Pemex (Mexico)

Section 7.2 "Política de financiamiento y estado de la deuda documentada" of Pemex's [2019 annual report](#) (pp. 88-93) presents information on Pemex's total debt, disaggregated by currency, by interest rate, by date of repayment/maturity and split between national and international debt-holders. However, this information is not broken down by specific debt instrument, although this is not required under EITI Requirement 2.6.a.i.

#### Pertamina (Indonesia)

Note 19a "Long-term liabilities" of PT Pertamina's [2019 consolidated financial statements](#) (pp. 93-95) describe the SOE's third-party debt financing in the form of bank loans (long-term liabilities). The information provided includes the principal of each loan, the identity of the lender, the range of interest rates effective in the year under review and the repayment modalities.

## Gaps with EITI disclosure requirements

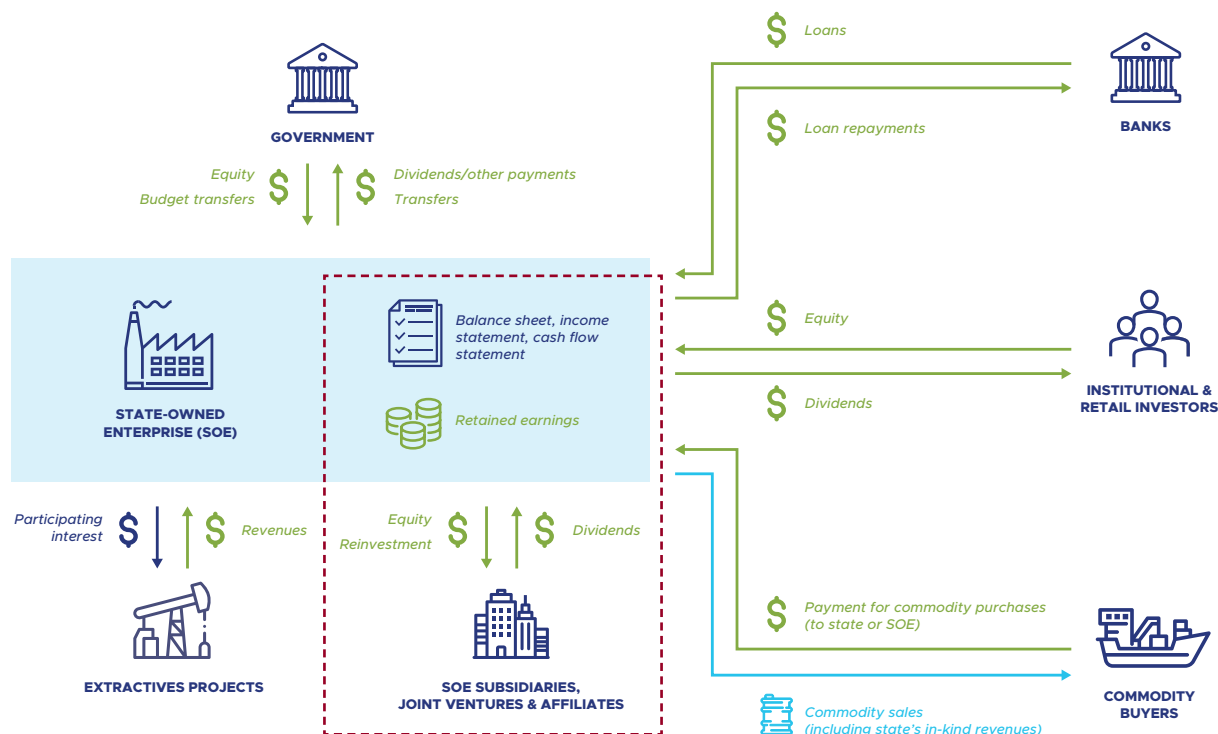
Consolidated financial statements often present details of a company's third-party debt financing in a consolidated manner, i.e. without disaggregation by type of third-party loan. While consolidated financial statements present the value of equity issued in the year under review, they do not always provide details on the identity of the new equity-holders. At a minimum, the EITI Standard requires public disclosure of SOEs' third-party financing in aggregate, not necessarily disaggregated by individual loan or equity-holder.

## How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of SOE third-party financing with a focus on analysis of the reasons for and terms of both debt and equity financing.
- Compare cash and accrual accountings of SOEs' third-party financing, which can strengthen public understanding of SOEs' financial management over several years.

## SOE(s)' financial relations with subsidiaries and joint ventures



SOEs often hold interests in other entities. These can be subsidiaries (in which an SOE has a controlling share), joint venture (a joint arrangement where two or more parties have joint control), or associate companies/affiliates (entities in which the SOE has a minority and non-controlling share).

**EITI Requirement 2.6.a.i****Rules and practices governing financial relations between SOE(s) and their subsidiaries and joint ventures**

In accordance with the EITI Standard, disclosures “*should include [...] transfers, retained earnings, reinvestment and third-party financing related to SOE joint ventures and subsidiaries.*”

The requirement aims to improve transparency of SOEs and their direct and indirect interests. The goal is to provide details about key figures for each subsidiary and joint venture, including any transfers of funds between the parent company and its interests.

The term “subsidiaries” refers to any entity in which an SOE has a controlling share (i.e. 50% + 1 share). The term “joint ventures” refers to a joint arrangement where two or more parties have joint control, and have rights to the net assets of that arrangement.<sup>2</sup> The terms “associate companies” and “affiliates” refer to entities in which the SOE has a minority and non-controlling share.

**Rules related to financial relations between SOE(s) and their subsidiaries and joint ventures****Where to find information**

The rules related to the financial relations between SOEs' subsidiaries, joint ventures and the parent SOE company are usually disclosed in the SOE's consolidated financial statements, under the notes section related to the summary of significant accounting policies. This section usually defines the accounting treatment of the SOE's investments in subsidiaries, joint ventures and associates/affiliates, including the SOE's entitlement to a share of the company's (subsidiaries, joint ventures and associates/affiliates) profits.

Complimentary to this information are the statutes of the relevant SOE subsidiaries, joint ventures and associates/affiliates, which usually provide information on the company's financial relations with its shareholder(s), including the SOE holding equity in the company.

**Gaps with EITI disclosure requirements**

The notes to the financial statements usually describe the types of accounting treatment per type of legal arrangement (e.g. subsidiary, joint venture, associate/affiliate) but do not always present a comprehensive list of companies in which the SOE holds equity, categorised by type of legal arrangement.

2 See IFRS (2017), “IFRS 11 Joint arrangements”, <https://www.ifrs.org/issued-standards/list-of-standards/ifrs-11-joint-arrangements/>.



## EXAMPLES

**GNPC (Ghana)**

Note 3.4 "Interests in joint arrangements" to GNPC's 2018 consolidated financial statements (pp. 19-20) describes the accounting policies related to GNPC's interests in joint arrangements, including joint operations, joint ventures and associates. These descriptions are in line with International Financial Reporting Standards (IFRS 11) and International Accounting Standards (IAS) 39.

The notes to the financial statements should confirm the type of legal arrangement for each company in which the SOE holds equity, even if this is not always centralised in one place in the audited financial statement. However, the notes to the financial statements may lack information on interests in subsidiaries or joint ventures held for sale or any discontinued operations.

## Practices related to financial relations between SOE(s) and their subsidiaries and joint ventures

**Where to find information**

The practices related to the financial relations between SOEs' subsidiaries, joint ventures and the parent SOE company are typically only partially described in audited financial statements. Information on dividends collected by SOEs from subsidiaries, joint ventures and affiliates in which they own equity interests is usually disclosed as part of the income statement, in the section on revenue and other income.

Additional information on retained earnings, reinvestments and third-party financing of SOE subsidiaries, joint ventures and affiliates is sometimes provided in the notes to the financial statements.

**EXAMPLES****GNPC (Ghana)**

Note 3.4 “Interests in joint arrangements” to GNPC’s [2018 consolidated financial statements](#) (pp. 19-20) describes the accounting policies related to GNPC’s interests in joint arrangements, including joint operations, joint ventures and associates. These descriptions are in line with International Financial Reporting Standards ([IFRS 11](#)) and [International Accounting Standards \(IAS\) 39](#).

Note 20a “Investment in joint ventures and associates” to GNPC’s 2018 consolidated financial statements (pp. 53-54) provides information on the dividends received by GNPC related to its equity interests in two joint ventures, Saltpond Offshore Producing Company (SOPCL) and GNPC-Technip Engineering Services. The information also includes each joint venture’s net profits after tax, from which it is possible to calculate the value of each joint venture’s retained earnings. These figures are presented on an accrual basis of accounting.

Additionally, transfers between GNPC and its related entities are detailed in Note 22 “Due from related parties” and Note 36 “Related party transactions”. However, most of the transactions or amounts due are not accompanied by an explanation or disaggregation of the transactions, which are provided in aggregate.

**KazMunayGas (Kazakhstan)**

Note 7 “Share in profit of joint-ventures and associates, net” to JSC National Company “KazMunayGas”’s [2019 consolidated financial statements](#) (p. 40) presents the value of net profits received by the SOE from its equity interests in joint ventures and affiliates. Note 19 “Investment in joint-ventures and associates” (pp. 52-61) presents information on the SOE’s investments in its joint ventures and affiliates, including summarised financial information (e.g. on assets, liability, equity, revenues and profit) for each joint venture and affiliate in which the SOE holds equity. These figures are presented on an accrual basis of accounting.

**Ecopetrol (Colombia)**

Annex 1 to Ecopetrol’s [2019 consolidated financial statements](#) (p. 101) provides an overview of the SOE’s ownership of different subsidiaries, including revenues derived by the SOE from each subsidiary in the period under review.

**Gaps with EITI disclosure requirements**

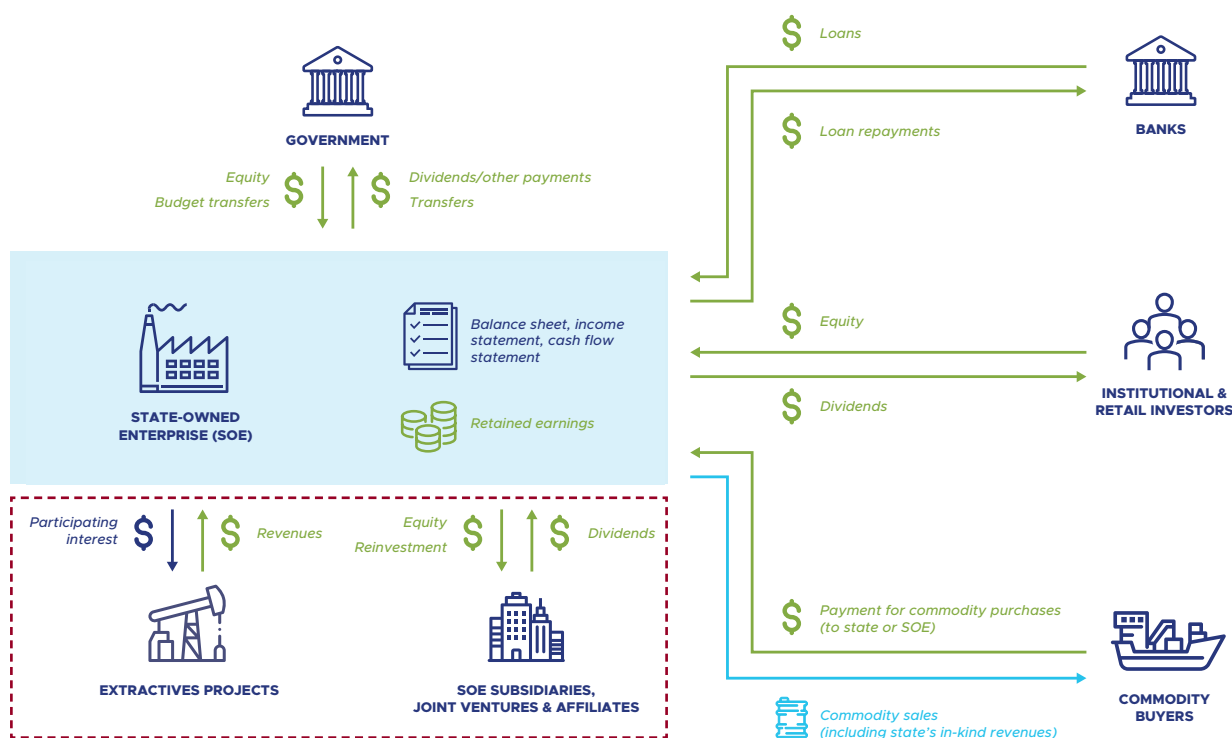
Consolidated financial statements usually present information on income (i.e. dividends) from equity participations in subsidiaries, joint ventures and affiliates in a consolidated manner (i.e. in aggregate for all companies). The notes to the financial statements sometimes present dividend income collected by SOEs broken down by individual company, although this is not always the case. The EITI Standard requires disclosures by individual entity or source of income, in which case it could also form part of the financial statement notes referring to “related party” transactions or disclosures.

## How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of SOEs' financial relations with their subsidiaries and joint ventures, with a focus on tracking transactions and revenues within the SOE group and at the consolidated group level.
- Provide a platform for analysis on the trends in subsidiaries and joint ventures' payments of dividends to the SOE group, to support public assessments of the SOE's return on investments in subsidiaries and joint ventures over time.

## 3. State and SOE ownership in the extractive industries



Ownership concerns the rights and duties of individuals that hold a legal or equitable interest in a company. Ownership information enables stakeholders to evaluate the nature of, and risks associated with, a company's interests in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity, and the effects of those interests on its financial position.

**EITI Requirement 2.6.a.ii****Government and SOE(s) ownership of mining, oil and gas companies, including terms and any changes**

In accordance with the EITI Standard, “implementing countries must disclose (...) [d]isclosures from the government and SOE(s) of **their level of ownership in mining, oil and gas companies operating within the country’s oil, gas and mining sector, including those held by SOE subsidiaries and joint ventures**, and any changes in the level of ownership during the reporting period.”

**Government and SOE(s) (including SOE subsidiaries and JVs’) ownership of mining, oil and gas companies****Where to find information**

Consolidated financial statements usually present the aggregate value of a company’s investments in joint ventures and affiliates as part of the balance sheet, under the “assets” section. Any impairments of investments in joint ventures and affiliates are presented as part of the income statement, under the “costs and expenses” section. A list of subsidiaries, joint ventures and affiliates in which the SOE holds equity interests may be provided in the notes to the consolidated financial statements, although such lists are not always comprehensive. In some cases, this list is disclosed in the supplementary information provided as part of the annual report.

Consolidated financial statements usually do not present a comprehensive list of equity interests held by an SOE’s subsidiaries, joint ventures or affiliates. Rather, consolidated financial statements usually show direct equity interests held by SOEs, not indirect equity interests held by companies in which the SOEs own a share.

**EXAMPLES****NNPC (Nigeria)**

Note 4 “Information about subsidiaries” of NNPC’s [2019 consolidated financial statements](#) (pp. 48-49) presents a comprehensive list of all of NNPC’s subsidiaries. Joint ventures are listed under Note 6.2 “Interest in joint-ventures and associates” (p. 51) and associates under Note 6.3 “Investment in associate” (p. 56). This information includes the specific equity interest held by NNPC and each company’s country of incorporation, but does not provide the terms attached to NNPC’s equity interest in each company.

**KazMunayGas (Kazakhstan)**

Note 19 “Investments in joint-ventures and associates” of JSC National Company “KazMunayGas”’s [2019 consolidated financial statements](#) (p. 52) present the list of companies in which the SOE holds equity, including the specific equity interest and details of the main activities of each company listed.

### Gaps with EITI disclosure requirements

Consolidated financial statements usually provide a list of the main subsidiaries, joint ventures and affiliates in which an SOE owns equity interests, but often present equity interests in small companies in aggregate form under a single category labelled "Other".

## Terms attached to government and SOE(s) ownership of mining, oil and gas companies

### Where to find information

The notes to the consolidated financial statements on the company's accounting policies usually provide information on the accounting treatment of assets and liabilities related to companies in which the company holds equity.

#### EXAMPLES

### GNPC (Ghana)

Note 3.4 "Interests in joint arrangements" of GNPC's [2018 consolidated financial statements](#) (pp. 19-20) provides information on the general terms attached to the SOE's equity interests in joint ventures and associates/affiliates, including its responsibility for its share of liabilities and expenses and its rights to its share of assets and revenues. This information is provided in general terms for all joint ventures and associates respectively, not disaggregated by individual joint venture and associate.

### Naftogaz (Ukraine)

Note 1 "The organisation and its operations" of [Naftogaz's consolidated financial statement for 2019](#) (p. 13) provides an overview of Naftogaz's principal subsidiaries and joint operations, though does not explicitly state the type of equity interest. Note 6 "Investments in associates and joint ventures" (pp. 25-26) provides information regarding Naftogaz's interests in affiliates/associates and other joint ventures, but also does not explicitly provide the terms of Naftogaz's equity stake in each company. Note 7 "Other non-current assets" highlights Naftogaz's expenses related to a soil exploration and development concession with another company, including its losses related to production sharing agreements. It refers to further details as part of Note 17 "Other operating expenses" (p. 39) and Note 26 "Summary of Significant Accounting Policies" (pp. 65-66). Naftogaz's [standalone 2019 financial statements](#) lists the same information under Note 5 "Long-term financial investments" (p. 28) and Note 6 "Long-term accounts receivable and other current assets" (pp. 29-30).

### Gaps with EITI disclosure requirements

Consolidated financial statements often provide the terms attached to the SOE's equity interests by type of company (e.g. subsidiary, joint venture, affiliate), but not consistently by individual company in which the SOE holds equity.

## Changes in government and SOE(s) ownership of mining, oil and gas companies

### Where to find information

Consolidated financial statements usually describe any changes in the SOE's ownership in subsidiaries, joint ventures and affiliates in the notes to the financial statements.

#### EXAMPLES

### Kumul Mineral Holdings Ltd (KMHL) (Papua New Guinea)

Note 2 "Restructure of the group and going concern" of KMHL's [2016 consolidated financial statements](#) (pp. 11-12), describes the SOE's restructuring in 2016, including the transfer of assets, including equity interests in extractive companies such as Eda Oil Ltd, and confirmation of the consideration paid in the transfer of each asset.

### Pertamina (Indonesia)

Note 4 "Acquisition, addition of participating interest and change in percentage of ownership" of PT Pertamina's [2019 consolidated financial statements](#) (pp. 51-58), describes the changes in the SOE's participating interests and equity interests, including considerations paid related to these changes.

### Gaps with EITI disclosure requirements

Information on changes in equity ownership by the SOE usually covers its direct equity participations, not necessarily changes in equity ownership held by the SOE's subsidiaries, joint ventures or affiliates. Indirect interests, e.g. interests of subsidiaries or associates/affiliates are normally not included.

## Terms of changes in government and SOE(s) ownership of mining, oil and gas companies

### Where to find information

Consolidated financial statements usually describe the terms of any changes in the SOE's ownership in subsidiaries, joint ventures and affiliates in the notes to the financial statements.

## EXAMPLES

**Equinor (Norway)**

Equinor's [2019 consolidated financial statements](#), under Note 4 'Acquisitions and disposals' (pp.175-177), presents information on Equinor's acquisitions and disposals of equity interests in companies and participating interests in oil and gas projects, including the value of the transaction and the financial consideration paid or received.

**Gaps with EITI disclosure requirements**

Information on changes in equity ownership by the SOE usually covers its direct equity participations, not necessarily changes in equity ownership held by the SOE's subsidiaries, joint ventures or affiliates. For tax authorities that are handling capital gains tax issues on transfer of ownership, challenges can emerge where these disclosures are made at a parent company level and not by the subsidiaries operating within the tax authorities' jurisdiction.

**How the EITI can add value**

EITI reporting can:

- Play a diagnostic role of all changes in state and SOE ownership of mining, oil and gas companies as well as participations in extractive projects over time.
- Improve transparency around the restructuring of SOE groups, in instances where the government implements wide-ranging restructurings of SOEs over several years.
- Clarify the state and SOEs' responsibilities for covering costs associated with SOE subsidiaries, joint ventures and affiliates over the course of the business cycle.

**4. State and SOE loans and guarantees****EITI Requirement 2.6.a.ii****Details of government and SOE(s) loans and guarantees to mining, oil and gas companies**

In accordance with the EITI Standard, *"where the government and SOE(s) have provided loans or loan guarantees to mining, oil and gas companies operating within the country, **details on these transactions should be disclosed**, including loan tenor and terms (i.e. repayment schedule and interest rate)."*

The term "loan tenor" refers to the length of the loan or debt instrument. The term "loan terms" refers to the repayment schedule (i.e. whether the loan is only repaid at maturity or whether the loan is amortised (paid off) over time, and if so the schedule of such repayments) as well as the interest rate (percentage charged on the total amount borrowed).

## Details of government loans and guarantees to mining, oil and gas companies

### Where to find information

Information on an SOE's third-party debt financing is usually disclosed as part of the balance sheet, in the section on (current and/or non-current) financial liabilities. Notes to the financial statement on related party transactions (which include the state as a related party) can include loans between the SOE and the government.

The notes to the financial statements usually describe any loans or loan guarantees received from the government, although this data is not consistently disaggregated by individual government loan or guarantee.

Information on government loans and (explicit) guarantees provided to specific companies is often found in the government's budget execution report and any reports published by the Ministry of Finance department responsible for debt management.

### EXAMPLES

#### Naftogaz (Ukraine)

Note 4 "Balances and transactions with related parties" of Naftogaz's [2019 consolidated financial statements](#) (p. 23) presents the aggregate value of government (sovereign) guarantees provided to Naftogaz at the end of 2018 and the end of 2019. The notes to the consolidated statement of financial position, in the section on liabilities (p. 7) and under Note 12 "Borrowings and Other Non-Current Liabilities" (pp. 32-33), provide additional information on these government guarantees, but only provides the aggregate value of Naftogaz borrowings guaranteed by the state, without specifying which precise third-party financial arrangements are covered by the state guarantee.

### Gaps with EITI disclosure requirements

Consolidated financial statements usually describe any loan and guarantee provided by the government, but this is often in aggregate terms, without details (e.g. tenor, repayment modalities or interest rate) of the specific loans guaranteed by the government.



## Details of SOE(s) loans and guarantees to mining, oil and gas companies

### Where to find information

Inter-company loans (e.g. loans from an SOE to its subsidiaries) are usually recorded in the financial statements of the subsidiaries, but not in the consolidated financial statements of the SOE group. However, company loans to joint ventures and affiliates are usually recorded in the company's consolidated financial statements in the cash flow statement, in the section related to "cash flow from investing activities". The terms of the company's loans to joint ventures and affiliates are sometimes described in the notes to the consolidated financial statements.

### EXAMPLES

#### SOCAR (Azerbaijan)

Note 37 "Contingences, commitments and operating risks" of SOCAR's [2016 consolidated financial statements](#) describes the guarantees provided by SOCAR to third parties, in the notes related to "Contingences, commitments and operating risks". The figures on SOCAR's guarantees to third parties are provided in aggregate (p. 77), with additional information on the company's commitments related to specific projects and companies (pp. 78-82).

#### GNPC (Ghana)

Note 22 "Due from related parties" of GNPC's [2018 consolidated financial statements](#) (p. 55) includes information on loans to related parties in 2017 and 2018, including to Saltpond Offshore Producing Co., Prestea Sankofa and GNPC Explorco. Note 36 "Related party transactions" (pp. 63-65) to the financial statements describe loans due from "related parties", including subsidiaries, joint ventures and affiliates of GNPC.

### Gaps with EITI disclosure requirements

Consolidated financial statements do not always list a company's loans to its own subsidiaries, although some statements do disclose this data. Information in financial statements on a company's loans to joint ventures and affiliates does not always include the loan tenor, interest rate and repayment modalities for each loan extended by the company.

## How the EITI can add value

EITI reporting can provide a framework for SOEs to disclose details of their loans and guarantees, as a key form of their accountability to the state and the general public. “Non-financial public corporations” (often mining or oil and gas SOEs) contributed to fiscal risk in some 60% of countries surveyed by the IMF in 2012.<sup>3</sup> Clarity on contingent liabilities such as loans and guarantees helps address concerns over fiscal transparency.

## 5. SOE expenditures

### EITI Requirement 2.6.c

#### Rules and practices related to SOE(s)'s operating and capital expenditures

In accordance with the EITI Standard, “implementing countries are encouraged to describe the rules and practices related to SOEs’ **operating and capital expenditures**.”

#### Rules and practices related to SOE(s)' operating expenditures

“Operating expenditures” denote the amount spent by an SOE relating to reoccurring overhead costs from day-to-day operations, i.e. expenses accruing from sales of oil, gas and products in a given year. These include:

- General, operating, selling, administrative and marketing costs
- Employee and facility expenses (i.e. rent)
- Exploration expenses if not capitalised (i.e. if the sources of funding for an expense are not clearly defined)
- Depreciation, impairment and amortisation (under the assumption it relates to a company's operations)
- Costs related to purchases of oil, gas and petroleum products

“Operating expenditures” do not include any tax or non-tax transfers to the state. They do not include financial costs (e.g. the cost, interest, and other charges related to the cost of finance, such as borrowing).

#### Where to find information

The rules related to SOEs' operating expenditures are not usually described in SOEs' audited financial statements. Rather, these rules are usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE's statutes or memorandum of incorporation.

3 IMF (2012), “Fiscal Transparency, Accountability, and Risk”, <https://www.imf.org/en/Publications/Policy-Papers/Issues/2016/12/31/Fiscal-Transparency-Accountability-and-Risk-PP4709>.

## EXAMPLE

**GNPC (Ghana)**

Note 15 “Petroleum projects” of GNPC’s [2018 consolidated financial statements](#) (p. 47) describe GNPC’s operating expenditures related to oil and gas projects. This data is broken down by project.

**Gaps with EITI disclosure requirements**

There are significant differences in the way in which SOEs (in different jurisdictions) report information on their expenditures. It is sometimes difficult to distinguish between operational and capital expenditures.

**Rules and practices related to SOE(s)’s capital expenditures**

“Capital expenditures” denote the amount in cash spent by an SOE on the purchase or upgrade of a fixed (physical) asset in a given year. In other words, the investments an SOE makes through acquisition or leasing of property, assets or equipment (wells, plants, etc.), or costs related to upgrading and maintaining existing assets to extend their life.

Essentially, “capital expenditures” denote any acquisition cost that is capitalised. Exploration activities, such as costs of drilling exploratory wells are only included when the SOE explicitly capitalises these costs. This indicator measures the investments an SOE makes into the future growth of the company.

**Where to find information**

The regulatory framework related to SOEs’ capital expenditures are not usually described in SOEs’ audited financial statements. The accounting policies described in the financial statements contain information on asset depreciation and amortisation. Rather, this regulatory framework is usually codified and described in relevant laws (e.g. a general SOE law, a law specific to a particular SOE, etc.) or the SOE’s statutes or memorandum of incorporation. However, the practice of an SOE’s capital expenditures in a given period will normally be disclosed as assets in the balance sheet and in the cash flow statement under investing activities.

## EXAMPLE

**Equinor (Norway)**

In Equinor’s [2019 consolidated financial statements](#), net capital expenditure and investment is found in the consolidated cash flow statement (p. 157). Information on capital expenditure can be found in the notes on “Property, plant and equipment” (p. 188) and in Note 4 “Acquisitions and disposals”. Equinor’s annual report provides some information on the rules related to the capital expenditure.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

Understanding financial statements of state-owned enterprises

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### Gaps with EITI disclosure requirements

There are significant differences in the way in which SOEs (in different jurisdictions) report information on their expenditures. It is sometimes difficult to interpret from SOEs' financial statements whether a cost has been capitalised, and to distinguish between operational and capital expenditures.

### How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of the extent to which SOEs' operating and capital expenditures are executed in accordance with the relevant rules and regulations.
- Provide a platform for assessing the trend of an SOE's capital expenditures over time, placing such data in the context of the SOE's overall financial performance and growth prospects.

## 6. SOE procurement and sub-contracting

### EITI Requirement 2.6.c

#### Rules and practices related to SOE(s)'s procurement

In accordance with the EITI Standard, *"implementing countries are encouraged to describe the **rules and practices related to SOEs' (...) procurement and sub-contracting.**"*

The term "procurement" refers to the acquisition of goods, services or works from an outside external source.

### Rules and practices related to SOE(s)'s procurement

#### Where to find information

Consolidated financial statements usually do not provide information on the rules or practices related to SOEs' procurement. However, some SOEs disclose this type of information on their corporate websites. An SOE's procurements may be covered under the general procurement legal framework of the respective state.

In instances where an SOE has undergone a performance audit, the subsequent performance audit report may include a review of the SOE's procurement rules and practices.

## EXAMPLES

**Equinor (Norway)**

Equinor's consolidated financial statements do not describe the rules and practices related to procurement. However, the Equinor website contains a section on "[Suppliers](#)" which provides information on the procedures, mechanisms, code of conduct as well as eAuction and eSourcing portals.

**Pemex (Mexico)**

Pemex's consolidated financial statements do not describe the rules and practices related to procurement. However, the Pemex website contains a section on "[Suppliers](#)", which provides information on the rules and procedures related to the SOEs' procurement and access to the "[Public information system suppliers and contractors](#)". Pemex has also recently launched a new [webpage](#) with information on all procurement and supplier contracts concluded by Pemex E&P, updated on a monthly basis.

**Gaps with EITI disclosure requirements**

While some SOEs disclose information on the rules related to their procurement on their corporate websites, this information usually focuses on the legal and regulatory procedures for procurement, rather than an overview of the actual practice.

**Rules and practices related to SOE(s)'s sub-contracting****Where to find information**

Consolidated financial statements usually do not provide information on the rules or practices related to SOEs' sub-contracting. However, some SOEs disclose this type of information on their corporate websites.

## EXAMPLE

**Pemex (Mexico)**

Pemex's consolidated financial statements do not describe the rules and practices related to procurement. However, the Pemex website contains a section on "[Contracting procedures](#)", which provides information on contracting procedures.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

Understanding financial statements of state-owned enterprises

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### Gaps with EITI disclosure requirements

While some SOEs disclose information on the rules related to their sub-contracting on their corporate websites, this information usually focuses on the legal and regulatory procedures for sub-contracting, rather than an overview of the actual practice.

### How the EITI can add value

EITI reporting can:

- Provide an annual diagnostic of the extent to which SOEs' procurement and sub-contracting are undertaken in practice in accordance with the relevant rules and regulations.
- Provide a platform for assessing the robustness of procurement and contracting policies and practices, with a view to reducing mismanagement and human discretion in the award of contracts.
- Provide a platform for aligning a company's contracting disclosure practices with applicable international standards, such as the Open Contracting Data Standard ([OCDS](#)).

## 7. SOE corporate governance

### EITI Requirement 2.6.c

#### Rules and practices related to SOE(s)'s corporate governance

In accordance with the EITI Standard, *"implementing countries are encouraged to describe the **rules and practices related to SOEs' (...) corporate governance**, e.g. composition and appointment of the **Board of Directors, Board's mandate and code of conduct.**"*

### Rules and practices related to SOEs' corporate governance (appointment of Board of Directors)

#### Where to find information

Consolidated financial statements usually do not provide information on the company's corporate governance, such as the appointment of the Board of Directors, although they often present information on the composition of the Board of Directors. However, some SOEs disclose some information on the appointment of the Board of Directors on their corporate websites. Where SOEs are regulated by a general SOE law or SOE-specific law, the appointment of the Board of Directors can be described in the relevant legislation.

**Gaps with EITI disclosure requirements**

Descriptions of the appointment of the Board of Directors on companies' websites tend to be cursory and focus on the statutory rules for the appointment of Board members, rather than the actual practice.

**EXAMPLE****National Oil Company of Kenya (Kenya)**

The National Oil Company of Kenya provides a brief description of the statutory rules for the appointment of Board Directors on its [website](#).

## Rules and practices related to SOEs' corporate governance (mandate of Board of Directors)

**Where to find information**

Consolidated financial statements usually do not provide information on the company's corporate governance, such as the Board of Directors' mandate. However, some SOEs disclose some information on the Board of Directors' mandate on their corporate websites. Where SOEs are regulated by a general SOE law or SOE-specific law, the mandate of the Board of Directors can be described in the relevant legislation.

**Gaps with EITI disclosure requirements**

The descriptions of the Board of Directors' mandate provided on corporate websites can often be quite succinct.

**EXAMPLE****KazMunayGas (Kazakhstan)**

While KazMunayGas's consolidated financial statements do not describe the rules or practices related to corporate governance, its [website](#) provides information on corporate governance rules, including the mandate of the Board of Directors.

## Rules and practices related to SOEs' corporate governance (code of conduct)

### Where to find information

Consolidated financial statements usually do not provide information on the company's corporate governance, such as the company's code of conduct. However, some SOEs disclose this type of information on their corporate websites.

#### EXAMPLE

### Naftogaz (Ukraine)

While Naftogaz's consolidated financial statements do not describe the rules or practices related to corporate governance, the SOE's [website](#) provides information on corporate governance, including the composition of its Board of Directors and reforms to its corporate governance in accordance with G20/OECD Principles of Corporate Governance.

### Gaps with EITI disclosure requirements

Codes of conduct are not always published on SOEs' corporate websites in full.

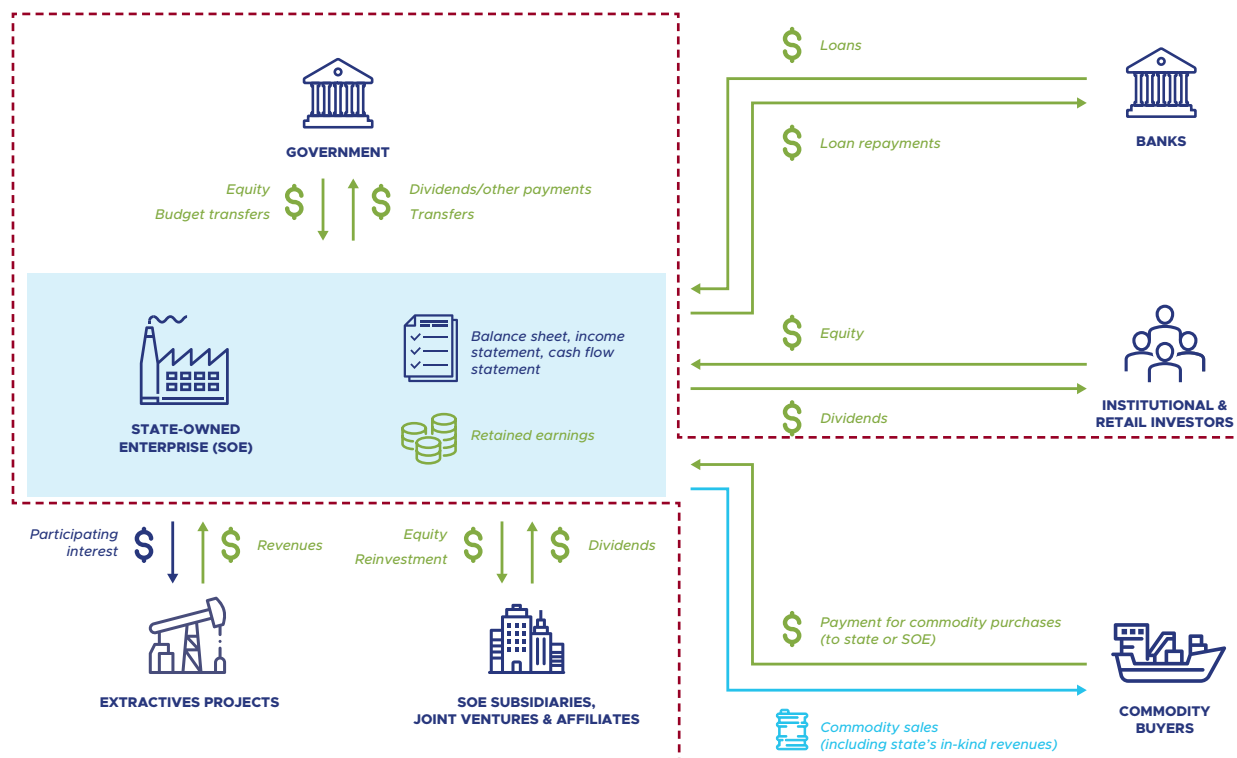
#### How the EITI can add value:

EITI reporting can:

- Provide more context on key aspects of SOEs' corporate governance, explaining the Board of Directors' appointment in practice, its mandate and governance structure and safeguards.
- Provide a platform for clarifying the decision making and accountability practices of SOEs.
- Provide a platform for aligning SOEs' corporate governance practices with international standards such as the OECD [Guidelines on Corporate Governance of State-Owned Enterprises](#), which provide further advice on how to strengthen SOE governance to improve competitiveness, efficiency and transparency.



## Requirement 4.2: Sale of the state's share of production or other revenues collected in kind



In many resource-rich countries, companies make in-kind payments to the government as fiscal payments in exchange for rights to extract resources. These payments are made through physical transfers of oil, gas and minerals, rather than cash.

## 1. In-kind revenues, proceeds of sales and transfers to the state

### EITI Requirement 4.2.a

#### In-kind revenue volumes received and sold by the state, proceeds of the sales and transfers of proceeds to the state

In accordance with the EITI Standard, “where the sale of the state’s share of production of oil, gas and/or mineral resources or other revenues collected in kind is material, the government, including state-owned enterprises, are required to disclose the **volumes received and sold by the state** (or third parties appointed by the state to sell on their behalf), the **revenues received from the sale**, and the revenues transferred to the state from the proceeds of oil, gas and minerals sold. The published data must be disaggregated by individual buying company and to levels commensurate with the reporting of other payments and revenue streams (Requirement 4.7).”

“In-kind revenues” consist of fiscal payments to government in-kind as a share of production. These types of arrangements are more prevalent in the oil and gas sector than in the mining sector.

Types of in-kind revenues collected by SOEs as fiscal agents on behalf of government (required by Requirement 4.2) include:

- **In-kind revenue from production sharing agreements (PSAs) (e.g. profit oil):** In a PSA, the state awards licenses to operators or a consortium, which take responsibility for operating the project (e.g. oil block). The operating group bears the risk and costs associated with exploration and production. It retains a share of production to cover its costs. The remaining “profit commodities” (e.g. “profit oil”) is divided between the operating group and the state as stipulated in the contract. In addition to its share of profit commodities, the government or SOE may receive an additional portion of production if it holds shares in the PSA (see “SOE as equity holder” below). Sometimes governments choose to receive profits from PSAs in monetary payments, but in-kind transfers are more common.
- **Service contract production:** Under service contracts, governments pay a company to extract commodities (such as oil) in exchange for a performance-based fee per volume of commodity produced (e.g. barrel of oil) that is often paid in kind. The state retains all of the production minus the amount that is paid to the company in fees.
- **“In-kind” payments of tax or royalty obligations:** Companies sometimes pay their tax and royalty obligations to the state with physical commodities (e.g. oil), rather than through monetary payments.

Shares of production collected by SOEs that do not constitute in-kind revenues collected on behalf of the state include:

- **Production from SOEs’ owned domestic fields and mines:** SOEs sell production from 100% SOE-owned extractive projects (e.g. oil fields, mines), or from jointly held fields where the SOE is the operator.

> continued on page 43

- **“Equity commodities”:** When a government or SOE is a non-operator participant in a joint venture, it can receive a share of production commensurate with its ownership share, often in kind. This would be subject to the terms of the joint venture agreement, which may lessen this share by the amount of costs incurred by the operator.
- **Profit and cost commodities:** When the SOE itself holds shares in a production sharing agreement (PSA), the SOE may receive an allocation of “cost commodities” (e.g. “cost oil”) to cover expenses it incurred in operating the field, and/or of “profit commodities” (e.g. “profit oil”), which is shared among contracting parties. This is distinct from PSA shares held by the government and managed by the SOE on the government’s behalf.

## Volumes of state in-kind revenues collected

### Where to find information

Consolidated financial statements usually provide information on the SOE’s share of oil production volumes, but not the volumes of in-kind revenues collected on behalf of the state with the SOE acting as a fiscal agent. However, some SOEs, such as Cameroon’s Société Nationale des Hydrocarbures (SNH), maintain a separate account of operations on behalf of the state and its own commercial interests, with two sets of audited financial statements.

### EXAMPLES

#### SNH (Cameroon)

SNH’s [website](#) presents summaries of two sets of financial statements: SNH-Etat, on behalf of the state, and SNH-Fonctionnement, on its own commercial account. The detailed notes to the consolidated financial statements are not publicly accessible. The same [webpage](#) presents the volumes of in-kind revenues collected by SNH-Etat from oil and gas companies’ operating producing blocks, in open data format (.xls).

#### GNPC (Ghana)

Note 5.1 “Summary of lifting for the year” of GNPC’s [2018 consolidated financial statements](#) (p. 36) describes GNPC’s crude oil liftings, which includes royalties and shares of carried and participating interest, but does not provide information on the in-kind oil revenues collected by GNPC on behalf of the state (as a fiscal agent). However, the “[Marketing](#)” section of GNPC’s website provides information on all crude oil liftings by GNPC, including of the government’s in-kind revenues collected by GNPC from oil and gas companies, disaggregated by company and by project, but not by type of government in-kind revenue flow (e.g. royalties, share of carried and participating interest). The Ministry of Finance [website](#) presents quarterly petroleum receipts and distribution reports with data on the volumes of government in-kind oil revenue per oil and gas company, but this is not disaggregated by in-kind revenue stream.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

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### EXAMPLE

#### NNPC (Nigeria)

NNPC's [website](#) presents monthly "Crude Oil Production Data" in open data format (.xls), with information on crude oil liftings in aggregate per type of arrangement (JV, PSC, independent, marginal fields, etc.) and on NNPC's crude oil liftings from each company operating oil and gas projects. However, this data is not disaggregated by revenue stream.

### Gaps with EITI disclosure requirements

Information on in-kind revenues in consolidated financial statements is usually presented in aggregate, not broken down by project. As for other financial flows, the EITI Standard requires that financial data imposed or levied on projects are disaggregated as such. Some SOEs that publish information on in-kind revenues, such as Cameroon's SNH, only publish summaries of their consolidated financial statements. Emerging best practice for SOEs' disclosures of their commodity sales consists of additional coverage of crude oil sales on their corporate websites.

## Volumes of state in-kind revenues sold

### Where to find information

Consolidated financial statements usually provide information on the volumes of crude oil sold, but not the volumes of the government's in-kind revenues sold on behalf of the state. However, some SOEs, like Cameroon's SNH, maintain separate accounts. Emerging best practice for SOEs' disclosures of their commodity sales consists of additional coverage of crude oil sales on their corporate websites.

### EXAMPLES

#### SNH (Cameroon)

SNH's [website](#) presents the volumes of in-kind revenues sold by SNH-Etat from oil and gas companies operating producing blocks, in open data format (.xls).

#### GNPC (Ghana)

GNPC's 2018 consolidated financial statements do not provide the volumes of crude oil sold by GNPC on behalf of the state. However, the "[Marketing](#)" section of GNPC's website provides information on all crude oil liftings by GNPC, including GNPC's sales of crude oil on behalf of the government, but not broken down by buyer. The "[Investor relations](#)" section of the GNPC website provides crude oil sales reports for 2015-2019 in open data format, disaggregating oil sales volumes by buyer and cargo with additional information on oil blend, vessel name, etc.

## EXAMPLES

**NNPC (Nigeria)**

NNPC's [website](#) presents monthly "Crude Oil Lifting Profiles" in open data format (.xls), with information on crude oil sales broken down by buyer and cargo.

**Pemex (Mexico)**

While Pemex's [website](#) only provides monthly and annual oil and gas production and sales figures in aggregate (without disaggregating the state's in-kind revenues specifically), the Mexican Petroleum Fund [website](#) presents data on volumes of in-kind revenues delivered to the state marketing company (broken down by crude oil, condensates and natural gas, but not by individual contract/project or in-kind revenue stream), the volumes of the state's in-kind revenues sold by the state marketing company (broken down by crude oil, condensates and natural gas, but not by individual buyer) and the value of proceeds of the sales by the state marketing company (in aggregate, not broken down by type of commodity nor by buyer).

**Gaps with EITI disclosure requirements**

Information on in-kind revenues in consolidated financial statements is usually presented in aggregate, not broken down by project. Some SOEs who publish information on in-kind revenues, such as Cameroon's SNH, only publish summaries of their consolidated financial statements.

**Value of proceeds of sales of state in-kind revenues****Where to find information**

Consolidated financial statements usually provide information on the value of proceeds of commodity sales, under the "Revenue" section of the income statement, but not explicitly the value of commodity sales on the government's behalf, nor broken down by buyer. However, some SOEs, like Cameroon's SNH, maintain separate accounts. Emerging best practice for SOEs' disclosures of their commodity sales consists of additional coverage of crude oil sales on their corporate websites.

## EXAMPLE

**NNPC (Nigeria)**

NNPC's [2019 consolidated financial statements](#) present the aggregate value of crude oil sales, but without breaking these down between revenues collected on behalf of the government and revenues collected on its own commercial account, nor by buyer. NNPC's [website](#) presents monthly "Crude Oil Lifting Profiles" in open data format (.xls), with information on crude oil sales broken down by buyer and cargo.

**EXAMPLES****SNH (Cameroon)**

SNH's [website](#) presents the value of crude oil sales by SNH-Etat on behalf of the state, albeit not broken down by buyer, in open data format (.xls).

**GNPC (Ghana)**

Payments for the sale of the state's in-kind revenues are made directly to the Petroleum Holding Fund, not to GNPC. The SOE's financial statements therefore do not present information on the value of proceeds of the sales of the state's in-kind revenues. GNPC's [2018 consolidated financial statements](#) provide the value of GNPC's net share of crude oil revenues and gas sales under the "Revenu" section of the income statement, as well as in Note 5 to the financial statements (p. 36), but do not present the value of the sales of the state's in-kind revenues. The "[Investor relations](#)" section of GNPC's website provides crude oil sales reports for 2015-2019 in open data format, disaggregating oil sales proceeds by buyer and cargo with additional information on oil blend, vessel name, etc.

**Gaps with EITI disclosure requirements**

Consolidated financial statements and annual reports usually do not present the value of proceeds of sales of the state's in-kind revenues broken down by buyer. However, where SOEs publish information on crude oil sales in a dedicated section of their corporate websites, this can include sales data disaggregated by buyer and cargo.

**Value of transfers to the state of proceeds of sales of state in-kind revenues****Where to find information**

Consolidated financial statements do not usually present information specifically on the transfer of proceeds of in-kind revenue sales to the state Treasury. This information is usually found in government accounts, such as the annexes to budget execution report where these are published by the Ministry of Finance.

**EXAMPLE****Ghana**

Payments for the sale of the state's in-kind revenues are made directly to the Petroleum Holding Fund, not to GNPC. The SOE's financial statements therefore do not present information on the value of proceeds of the sales of the state's in-kind revenues. The Ministry of Finance [website](#) presents quarterly petroleum reports that present the value of transfers of the proceeds of crude oil sales by GNPC to the Petroleum Fund.

### Gaps with EITI disclosure requirements

While SOEs' consolidated financial statements present the value of payments to the state of taxes and dividends, they usually do not include the value of transfers of proceeds of in-kind revenue sales specifically.

In some cases, SOEs lump payments of the proceeds of sales of the state's in-kind revenues into operational expenditures without providing disaggregated information.

### How the EITI can add value

EITI reporting can:

- Enable SOEs to demonstrate the efficiency of the commercialisation process for the commodities they produce.
- Provide a platform for annual diagnostics of the terms of trade for the state's commodity sales, allowing for multi-year and cross-country comparisons of commodity sales prices and terms.

## 2. Buyer selection process and sales agreements

### EITI Requirement 4.2.a

#### Rules and practices for selecting buyers of the state's in-kind revenues

In accordance with the EITI Standard, “implementing countries including state-owned enterprises are encouraged to disclose a description of the **process for selecting the buying companies**, the technical and financial criteria used to make the selection, the list of selected buying companies, any material deviations from the applicable legal and regulatory framework governing the selection of buying companies, and the **related sales agreements**.”

### Rules for selecting buyers of the state's in-kind revenues

#### Where to find information

Neither SOEs' consolidated financial statements nor annual reports usually describe the statutory process for selecting buyers for commodity sales. This information can at times be published separately on the SOE's website.

#### EXAMPLE

### NNPC (Nigeria)

While NNPC's [website](#) presents only a cursory description of the buyer selection process, a [2019 presentation](#) by NNPC (published on a third-party website) presents an overview of the company process for selecting buyers for its crude oil exports.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

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### Gaps with EITI disclosure requirements

Information on the statutory rules for selecting buying companies is often not published on SOE websites.

## Practices related to selecting buyers of the state's in-kind revenues

### Where to find information

Neither SOEs' consolidated financial statements nor annual reports usually describe the practice of buyer selection for commodity sales. Information on the identity of commodity buyers is seldomly published separately on the SOE's website.

#### EXAMPLE

### Pemex (Mexico)

Pemex's trading subsidiary, PMI Comercio Internacional, has a standalone [website](#) with information on general terms and conditions, pricing and commercial guidelines.

### Gaps with EITI disclosure requirements

While some SOEs disclose information on the rules related to their buyer selection on their corporate websites, this information usually focuses on the legal and regulatory procedures for buyer selection, rather than an overview of the actual practice. Information on practical deviations from the rules for selecting buying companies is often not published on SOEs' websites.

## Sales agreements related to the sale of the state's in-kind revenues

### Where to find information

When publicly available, crude oil sales contract templates are sometimes published on the corporate websites of SOEs. The final versions of commodity sales contracts are often not publicly available.



## EXAMPLES

**SOMO (Iraq)**

While not published on the SOMO or Ministry of Oil website, the template crude oil sales contract was published in Appendix 6 of Iraq's [2012 EITI Report](#) (pp. 170-190).

**National Hydrocarbons Commission (Mexico)**

The oil and gas regulator CNH publishes on its [website](#) the annual crude oil marketing contract it concludes with marketers for the sale of the government's in-kind oil revenues. However, the crude oil sales agreements concluded between the marketer and buyers are not publicly disclosed.

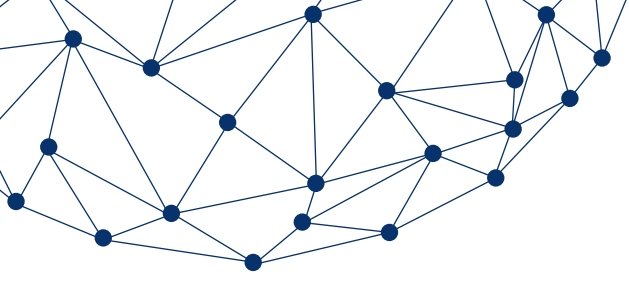
**Gaps with EITI disclosure requirements**

Commodity sales agreements are usually not published by SOEs.

**How the EITI can add value**

EITI reporting can:

- Help SOEs ensure a level playing field for all market participants through transparency in the practice of the sales process.
- Improve transparency on the ownership of contractors and help clarify the relationship between the SOE and its business partners, and reduce counterparty risk. This in turn can improve the SOE's credibility with lenders and the investment community.
- Provide a platform for aligning buyer selection practices with international standards such as the OECD's guidance for state-owned enterprises on "[How to Select Buyers of Oil, Gas and Minerals](#)", which provides further advice on how SOEs can develop transparent and competitive buyer selection procedures.



# Requirement 4.5: Transactions related to SOEs

## EITI Requirement 4.5

### Company payments to SOE(s) and transfers between SOE(s) and government

In accordance with the EITI Standard, “the multi-stakeholder group must ensure that the reporting process comprehensively addresses the role of SOEs, including comprehensive and reliable disclosures of material **company payments to SOEs, SOE transfers to government agencies and government transfers to SOEs.**”

“Company payments to SOEs” refers to revenue collection by SOEs on behalf of the state, whether through fiscal instruments (e.g. royalties) or through ownership (e.g. dividends).

## 1. Company payments to SOEs

### Where to find information

Consolidated financial statements present the value of dividends received from subsidiaries, joint ventures and affiliates in the “revenue” section of the income statement.

#### EXAMPLE

### GNPC (Ghana)

GNPC’s [2018 consolidated financial statements](#) (pp. 8 and 13) and Note 20 “Investment in associates and joint-ventures” (pp. 54-55) provide the value of dividends received from all subsidiaries, joint ventures and other affiliate companies. The financial statements present the aggregate value of revenues from oil and gas operators as contributions to the training and technology fund, but not disaggregated by company. These figures are presented on an accrual basis of accounting.

**Gaps with EITI disclosure requirements**

The information on dividends from subsidiaries, joint ventures and affiliates is not always broken down by individual company.

**2. SOE transfers to the government****Where to find information**

Information on SOE transfers to the government, including dividends to the state, are usually disclosed as part of the SOE's balance sheet, in the section related to "shareholder equity". Transfers of net profits from the SOE to the state are usually categorised as "distribution of profits" or "statement of stockholders' equity as a subtraction from retained earnings", among other labels.

**EXAMPLES****Qatar Petroleum (Qatar)**

The summary of 2018 consolidated financial statements included in [QP's 2018 Annual Review](#) provides the value of dividends transferred by QP to the Ministry of Finance (pp. 78-79), other charges related to the Ministry of Finance (p. 80) and cash transfers to the Ministry of Finance (p. 81). These figures are presented on an accrual basis of accounting.

**SNPC (Republic of Congo)**

Note 34 "Fiche de synthèse des principaux indicateurs financiers" of SNPC's [2018 financial statements](#) (p. 53) presents the value of dividends declared based on the 2017 and 2018 financial results. These figures are presented on an accrual basis of accounting. In cash-accounting terms, SNPC did not pay any dividend to its sole shareholder (the state) in either 2017 or 2018.

**Gaps with EITI disclosure requirements**

Not all companies record the components of operating income in detail, so some report data for "operational costs" that also includes non-tax transfers to government.

SOEs sometimes do not report dividend payment, which could mean that they either did not pay dividends or that dividends were subsumed under other line items on the financial report.

There are differences in figures presented for SOE dividends between data presented on an accrual basis of accounting (dividends related to profit recorded for that year) and cash basis of accounting (dividends paid in that year, usually related to profits recorded in a previous year).

### 3. Government transfers to SOEs

#### Where to find information

Information on transfers from the government to the SOE are usually disclosed as part of the cash flow statement, under “Financing Activities”. Government transfers to SOEs can be categorised as government “grant”, “assistance” or “other income from the state”, among other labels.

#### EXAMPLE

##### Pemex (Mexico)

Pemex's [2014 consolidated financial statements](#) presents the value of financial transfers from the Federal Government of Mexico to Pemex, categorised as “Increase in equity due to Mexican Government contributions” under “Financing Activities” (pp. 7 and 102). These figures are presented on an accrual basis of accounting.

#### How the EITI can add value

EITI reporting can:

- Help clarify the flow of fiscal revenues collected by an SOE through to its transfers to the government treasury.
- Help companies clarify their subsidies across the group between loss-making and dividends collected from profitable subsidiaries, joint ventures and affiliates.
- Provide context and insight on other payments made to and received by SOEs beyond the revenue flows codified in relevant laws and regulations (for example, “advances on fiscal payments” made to government by certain SOEs in the DRC).

# Requirement 6.2: SOE quasi-fiscal expenditures

## EITI Requirement 6.2

### Quasi-fiscal expenditures by SOEs

In accordance with the EITI Standard, “implementing countries must include **disclosures from SOEs on their quasi-fiscal expenditures**. The multi-stakeholder group is required to develop a reporting process with a view to achieving a level of transparency commensurate with other payments and revenue streams, and should include SOE subsidiaries and joint ventures. Quasi-fiscal expenditures include arrangements whereby SOEs undertake public social expenditure such as **payments for social services, public infrastructure, fuel subsidies and national debt servicing**, etc. outside of the national budgetary process.”

## 1. Social services quasi-fiscal expenditures by SOEs

### Where to find information

Consolidated financial statements usually do not disclose quasi-fiscal expenditures categorised as such. Expenditures that are not part of the SOE's core mandate can at times be highlighted in the auditor's opinion on the financial statements, in cases where the independent auditor questions the legal or contractual basis on which these expenditures are made. In these cases, quasi-fiscal expenditures may be described as part of the “expenditure” section of the income statement, although not labelled as such.

Expenditures by SOEs on behalf of government whose expected reimbursement by government has not yet been received can sometimes be disclosed as “related party transactions/balance”, given that the state is considered a related party to the SOE as a shareholder.

Expenditures by SOEs on social services can sometimes be reported as part of the “expenditure” section of the income statement, but are usually not clearly distinguished from conventional social expenditures, either mandatory (by law or contract) or voluntary.

It is usually the government that directs SOEs to undertake quasi-fiscal expenditures, although in some instances directions by individual government officials may not be codified in relevant laws and regulations. Expenditures that have not been directed by the government and are related to assets that are owned or under the control of the SOE usually do not fall under the definition of quasi-fiscal expenditures. See more information in the EITI's [Guidance Note on quasi-fiscal expenditures](#).

**EXAMPLE****Equinor (Norway)**

By EU Law, Equinor and other extractive companies report on payments to governments which include these types of expenditures in the countries they operate. These are reported as “fees” in Equinor’s [annual report](#) (p. 288), but are not broken down by individual type of social expenditure, nor beneficiary.

**Gaps with EITI disclosure requirements**

Consolidated financial statements usually do not present the detail of expenditures disaggregated by project or type, meaning that specific quasi-fiscal expenditures on social services are not usually visible without the detail of the SOE’s expenditures.

## **2. Public infrastructure quasi-fiscal expenditures by SOEs**

**Where to find information**

Consolidated financial statements usually do not disclose quasi-fiscal expenditures categorised as such. Expenditures that are not part of the SOE’s core mandate can at times be highlighted in the auditor’s opinion on the financial statements, in cases where the independent auditor questions the legal or contractual basis on which these expenditures are made. In these cases, quasi-fiscal expenditures may be described as part of the “expenditure” section of the Income statement, although not labelled as such.

Expenditures by SOEs on public infrastructure can sometimes be reported as part of the “expenditure” section of the Income statement, particularly where the value of such expenditures is large. However, these types of expenditures can often be aggregated with conventional social expenditures, either mandatory (by law or contract) or voluntary, and not clearly highlighted in the SOE’s financial statements.

**EXAMPLE****SOCAR (Azerbaijan)**

Note 27 “Charter capital, additional paid-in-capital, retained earnings and gain on sale of subsidiary share” of SOCAR’s [2016 consolidated financial statements](#) (p. 68) describes SOCAR’s financing of construction and repair works on recreational, transport, educational and medical infrastructure on behalf of the Government of Azerbaijan. The financial statements provide the aggregate value of these expenditures in the year under review, but do not disaggregate this data by project or type of expenditure.

## EXAMPLES

**OMNIS (Madagascar)**

The audit report on OMNIS's [2018 financial statements](#) (p.5) raises concerns over MGA 7.58 billion in the SOE's expenditures on the construction of a new public highway to the capital city's airport, which the auditor claims has undermined the SOE's autonomy. The audit report confirms that the expenditure was undertaken at the direction of two government ministers, who asked for OMNIS to cover these construction expenses on behalf of the state.

**SNIM (Mauritania)**

In Mauritania, the mining SOE (SNIM) paid the contractor for the development of Nouakchott's new airport directly and is gradually reimbursed by the state through deductions from its tax (unique royalty payment) payments to the government in subsequent years. These deductions by SNIM from its payments to government are not recorded in the national budget. Note 4.3.1 "Investment in associate's entities" of SNIM's [2017 consolidated financial statements](#) (p.27) describes the SNIM loan to the NJAH construction company, to be reimbursed by the state.

**Gaps with EITI disclosure requirements**

Consolidated financial statements usually do not present the detail of expenditures disaggregated by project or type, meaning that specific quasi-fiscal expenditures on public infrastructure are usually not visible without the detail of the SOE's expenditures.

**3. Subsidies quasi-fiscal expenditures by SOEs****Where to find information**

Consolidated financial statements usually do not disclose quasi-fiscal expenditures categorised as such. Expenditures that are not part of the SOE's core mandate can at times be highlighted in the auditor's opinion on the financial statements, in cases where the independent auditor questions the legal or contractual basis on which these expenditures are made. In these cases, quasi-fiscal expenditures may be described as part of the "expenditure" section of the income statement, although not labelled as such.

Subsidies provided by SOEs are not usually reported as such unless they are reimbursed by the national government (e.g. in Indonesia). Off-budget subsidies (not reimbursed by the national government) tend to only be evident in the price of sales of commodities to specific customers, and need to be calculated based on the difference with market prices.

**EXAMPLES****North Coal Enterprise (Afghanistan)**

The SAO [audit report](#) of NCE's 2016-2017 financial statements (Issue 2, p. 3) raised concerns over the lack of adjustment of NCE's sales prices since 2008, noting that a Council of Ministers decision allowed NCE to adjust sales prices in light of market demand. The SAO recommended that NCE establish a transparent and competitive pricing mechanism that would lead to increased revenues for NCE.

**Naftogaz (Ukraine)**

Naftogaz of Ukraine NJSC (NAK) supplies natural gas to domestic power plants that produce thermal heat to consumers, at prices below domestic market prices for natural gas. Under the 2015 Law on the Natural Gas Market, domestic natural gas sales are conducted on the basis of market prices, with the exception of natural gas sales to household consumers, religious organisations and thermal heat and electricity producers. The price of natural gas supplied to these three types of consumers are regulated by CMU Resolution No. 758 and CMU Resolution No. 187, which set prices below the prevailing domestic market prices for natural gas.

Naftogaz does not receive compensation from the government budget for the foregone revenue related to these subsidised sales. Note 2 "Operating Environment" of Naftogaz's [2019 consolidated financial statements](#) (pp. 18-19) describes the lack of government compensation for these public service obligations, including the value of such off-budget subsidies by Naftogaz in 2019.

**Gaps with EITI disclosure requirements**

Consolidated financial statements rarely highlight subsidies as a standalone cost, unless these are fully reimbursed by the national government. The detail of below-market sales prices is usually only highlighted in the auditor's report.

**4. National debt servicing quasi-fiscal expenditures by SOEs****Where to find information**

Consolidated financial statements usually do not disclose quasi-fiscal expenditures categorised as such. Expenditures that are not part of the SOE's core mandate can at times be highlighted in the auditor's opinion on the financial statements, in cases where the independent auditor questions the legal or contractual basis on which these expenditures are made. In these cases, quasi-fiscal expenditures may be described as part of the "expenditure" section of the income statement, although not labelled as such.

Payments for sovereign debt provided by SOEs are not usually reported as such in consolidated financial statements. Payments for national debt not reimbursed by the national government tend to only be evident in the financial statements of the specific subsidiary or special purpose vehicle servicing the debt.



## EXAMPLE

**Kumul Petroleum Holdings (Papua New Guinea)**

The oil company Oil Search Ltd, which is listed on the Australia Stock Exchange, submitted a [public filing](#) that disclosed the change of ownership of 10% of its shares in February 2016, which were transferred to the SOE Kumul Petroleum Holdings. The 10% equity interest in Oil Search had been used as collateral for a AUD 1.2 billion loan from UBS to the Government of PNG to fund its interest in the PNG LNG project operated by ExxonMobil since 2014.

This UBS loan was novated to Kumul Petroleum Investment Ltd. (a subsidiary of the Kumul Petroleum Holdings) in February 2016, at the same time as the Oil Search shares were transferred. This effectively moved the debt off of the government's balance sheet, given that KPH does not receive an explicit sovereign guarantee. Given that KPH was the entity receiving dividends from the PNG LNG project, it retained earnings (dividends) from that project to pay off the loan, which was completed in late 2017.

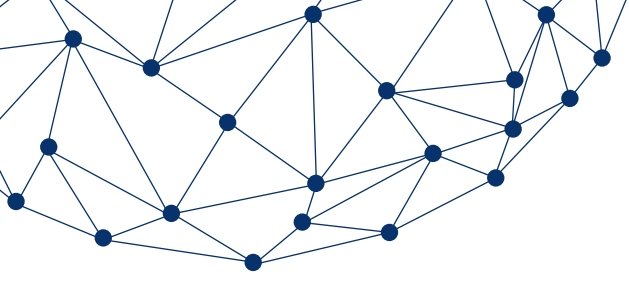
**Gaps with EITI disclosure requirements**

Payments for national debt can involve deductions from the state's in-kind revenues that are not recorded in the SOE's financial statements. In other cases, payments for national debt are transferred to one of the SOE's subsidiaries so that it can deduct government revenues to service the debt.

**How the EITI can add value**

EITI reporting can:

- Provides a unique framework for SOEs to structure their disclosures of quasi-fiscal expenditures they may be asked to undertake. Disclosures in line with the EITI Standard allow SOEs to publicly clarify the non-commercial activities and costs they are subject to, as context for the broader public assessment of SOEs' efficiency and profitability.
- Provide a platform for dialogue and resolution between different stakeholders including SOEs, government (Ministry of Finance, line ministries), civil society and others on issues of public finance management including quasi-fiscal expenditures outside of the conventional budgetary process.
- Help countries demonstrate progress against benchmarks for support from the international community, such as programmes with the IMF.



# Annex: Glossary of common terms in audited financial statements

## **Accounting policies**

Accompanying any set of financial statements are the notes to the financial statements, which provide the reader with more information about the organisation's operations and the figures presented in the financial statement. The second note typically describes the organisation's accounting policies. These policies refer to the specific principles, practices and rules applied by an entity in preparing and presenting financial statements.

## **Auditor's report**

The auditor's report is a formal opinion, or disclaimer of opinion, issued by an auditor after performing an audit. To provide an audit opinion, the independent auditor must obtain sufficient and appropriate evidence to confirm that the financial statements are free from material error or omission. Essentially, this report specifies whether an independent expert found any errors or omissions that could impact the reader's understanding of the financial statement. The auditor's report typically follows the table of contents for the financial statements.

## **Balance sheet**

A balance sheet, also called "Statement of financial position" is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating a company's capital structure.

## **Cash flow statement**

A cash flow statement is a financial statement that summarises the amount of cash and cash equivalents entering and leaving a company. The cash flow statement measures how a company manages its cash position, meaning how it generates cash to pay its debt obligations and fund its operating expenses.

## **Cash-based vs accrual-based accounting**

A cash basis of accounting is a method of accounting that recognises revenues and expenses at the time cash is received or paid out. An accrual basis accounting recognises income at the time the revenue is earned and records expenses when liabilities are incurred, regardless of when cash is received or paid.

## **Income statement**

The income statement, also called “profit and loss (P&L) statement”, is the most common financial statement and summarises a company's revenues, costs and expenses incurred during a specified period, usually a fiscal quarter or year.

## **Joint ventures vs joint arrangements**

The key distinction between a joint venture and a joint arrangement/operation is that a joint venture has rights to the net assets of a joint venture. In contrast, for a joint operation, the parties that have joint control over the arrangement have rights to the assets, and obligations for the liabilities, of the arrangement ([IFRS 11](#)).

## **Materiality**

Material is the term that refers to whether information carries enough significance to influence decisions. It can be either quantitative or qualitative. For example, if a company generates millions of dollars in revenue, an amount of USD 0.50 is not quantitatively material. Generally Accepted Accounting Principles (GAAP) require that all material considerations be disclosed. For example, a quantitative materiality consideration is usually a specific percentage of net income or other major financial aggregate, such as 5% of net income from continuing operations or 2-3% of operating income, but these thresholds can vary significantly. However, an item cannot be considered as immaterial only because it is below a predetermined quantitative threshold. Other qualitative factors may still make an item material, such as misstatements that affect key ratios, or where statements distort transactions with related parties or other specific matters (see [IFRS Materiality practice statement](#)).

## **Ownership or interests in other entities**

Ownership concerns the internal organisation of a business entity and the rights and duties of the individuals holding a legal or equitable interest in that business. Ownership information enables users of a company's financial statements to evaluate the nature of, and risks associated with, its interests in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity, and the effects of those interests on its financial position, financial performance and cash flows (IFRS12).

## **Reinvestment vs investment**

Reinvestment is when income distributions received from an investment are ploughed back into that investment instead of receiving cash. Reinvestment works by using dividends received to purchase more of that stock, or interest payments received to buy more of that bond.

## EITI REQUIREMENTS 2.6, 4.2, 4.5 AND 6.2

Understanding financial statements of state-owned enterprises

Guidance on using SOEs' financial statements as a starting point for public disclosures

### Related parties

A related party is a person or an entity that is related to the reporting entity. A “person” or a close member of that person’s family is related to a reporting entity if that person has control, joint control or significant influence over the entity or is a member of its key management personnel. An “entity” is related to a reporting entity if, among other circumstances, it is a parent, subsidiary, fellow subsidiary, associate or joint venture of the reporting entity, or if it is controlled, jointly controlled, or significantly influenced or managed by a person who is a related party ([IAS24](#)).

### Retained earnings

Retained earnings are the accumulated portion of a business’s profits that are not distributed as dividends to shareholders but are instead reserved for reinvestment back into the business. Normally, these funds are used for working capital and fixed asset purchases (capital expenditures) or allotted for paying off debt obligations. Retained earnings are found from the bottom line of the income statement and then carried over to the shareholder’s equity portion of the balance sheet, where they contribute to book value. Retained earnings (RE) are calculated as follows:  $RE = \text{Period Start RE} + \text{Net Income/Loss} - \text{Cash Dividends} - \text{Stock Dividends}$ .

### Statement of shareholders’ equity

The statement of shareholders’ equity is a financial document that a company issues as part of its balance sheet. It highlights the changes in value to stockholders’ or shareholders’ equity, or ownership interest in a company, from the beginning of a given accounting period to the end of that period.

### Stock

A stock is calculated as follows:  $\text{Stock} = \text{Assets} - \text{Liabilities} + \text{Shareholder Equity}$  (stock). Based on the equation, the common stock, being shareholder equity, is neither an asset nor a debt. However, being on the opposite side of the asset equation, it is treated much more like a liability than an asset. The reason is that a shareholder can request to cash out.

### **Subsidiaries versus associates/affiliates**

Affiliate, associate and subsidiary are all terms referring to the degree of ownership that a parent company holds in another company. In most cases, affiliate and associate both describe a corporation whose parent only owns a small stake in the company. Conversely, a subsidiary is a company whose parent is a majority shareholder.

An associate is an entity over which the investor has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee without the power to control or jointly control those policies. If an entity holds, directly or indirectly (e.g. through subsidiaries), 20% or more of the voting power of the investee, it is presumed that the entity has significant influence ([IFRS IAS 28](#)).

### **Third-party financing**

A third party is an individual or entity that is involved in a transaction but is not one of the principals (i.e. not the company or one of its shareholders, such as the state). Third-party financing occurs when the financing for the SOE comes from a third party, such as a bank or private investor.



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