# Advancing State-Owned Enterprise Transparency through the EITI

**Background paper for the EITI Strategy Working Group**

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## 1. The Importance of Disclosures by State-Owned Enterprises (SOEs)

SOEs control some of the most significant revenue flows generated by oil and mineral production. In the petroleum sector, they are typically responsible for the sale of oil the state gains by virtue of production sharing contracts or equity shareholdings. These sales often dwarf other revenue streams generated by extractive industries. They bring in over two thirds of *total government revenue* in countries including Azerbaijan, Congo-Brazzaville, Iraq and Yemen. Even in Norway, with a significantly more diversified economy, export sales equal 14 percent of the national budget.

In addition to their role selling government crude, SOEs often bear responsibility for collecting various financial contributions from private oil companies, including signature bonuses, dividends, area fees and training fees. When they privatize or sell shares, they bear responsibility for monetizing some of the most important resource-backed assets in the state's possession.

SOEs often execute large-scale social expenditures outside the traditional mandate of an oil or mining company. In Azerbaijan and Kazakhstan, national oil companies have been charged with activities including construction of schools and clinics and aid to vulnerable populations. In the DRC, the role of state mining company Gécamines far exceeds its commercial functions as one of the country's biggest employers and the backbone of the economy and social structure in copper-producing regions.

The retention or transfer of funds to cover the operations of SOEs can also have powerful impacts on the amount of money that accrues to the state from extractive activity. Forty-six percent of all oil revenues generated in Ghana through the first ten months of production were transferred to the Ghana National Petroleum Corporation to fund its activities.

Despite the size of their activities and revenue flows, many of SOE activities remain opaque, with serious consequences for natural resource governance. In Nigeria, the Finance Ministry overestimated oil revenues by 39% in the 2011 budget due in large part to non-remittance of funds by the NOC. In Angola, poor reporting by the national oil company on its revenue and the expenditures it carried out on the state's behalf were key causes of $32 billion public accounting gap, representing ¼ of total national GDP between 2007 and 2010. In the DRC, Gécamines sold its shares in two large joint ventures 2011 without a public tender to a business associate of the President, for a reported cost ($137 million) that some analysts have put at one-eighth of their true market value ($1.1 billion).[1]

## 2. Existing Practice on SOE Revenue and Payment Disclosure

[1] Elisabeth Caesens, *National Mining Company Research—The Case of Gécamines in the Democratic Republic of Congo*, Revenue Watch Institute, forthcoming (2012).

Several EITI-implementing countries include information on payments received by SOEs in their reports, but with varying degrees of quality and detail. Albania's report includes transfers to and from SOEs in the aggregated numbers, but this is of limited value to citizens in assessing the performance of and leakages from the SOE itself (see related brief on the benefits of disaggregated reporting).

Other EITI implementing countries provide more detail. Cameroon's 2006-08 report, for example, reports on the national oil company's receipt of royalties, signature bonuses, dividends and training fees, its share of barrels produced and its transfers to the treasury. Cote d'Ivoire's 2007-08 report reconciles statements about the value of transfers of oil and gas between private partners and the SOE, and the SOE's tax and dividend payments to the state. The DRC's 2007 report provides information on various tax and other payments by Gecamines and Sodimico.

These reports demonstrate the feasibility of providing SOE-specific EITI reconciliations. But there is a clear need for uniform standards. Some countries—including such notable EITI implementers as Azerbaijan and Kazakhstan—provide virtually no meaningful information about the activities or revenue flows associated with state-owned companies. In such cases, EITI reports do not provide information about the level of oil revenues available for spending by government—a founding purpose of EITI.

Beyond EITI, many state-owned enterprises publish significant information about their activities and finances, particularly but not exclusively companies that are partially listed on stock exchanges. These cases can provide useful examples for EITI implementers. Audited financial statements and annual reports are published by a large number of companies including StatoilHydro (Norway), Pemex (Mexico), Petrobras (Brazil) and Petroecuador (Ecuador). These companies and others also publish thorough (disaggregated) data on their payments to government and data on their costs of operation.

**3. Implementing SOE reporting in the EITI**

The following disclosures should be mandatory for all EITI participating countries with state-owned petroleum or mining companies, as they fall within the existing scope of EITI's principles and criteria:

A. **Reconciliation of all material revenues received by the state-owned enterprises.** This reporting would follow the same form as typical EITI reporting, with companies providing payment data and the SOE providing receipt data for revenue streams which it collects. Depending on the country, these could include:
    - Bonuses
    - Royalties (in most cases royalties are not paid directly to the SOE, but there are some cases such as the DRC wherein a contractual royalty does come to the company)
    - Area fees/surface rentals
    - Dividend payments from joint ventures in which the SOE holds equity to the SOE
    - Petroleum or minerals received by the SOE pursuant to production sharing agreements or other contractual clauses (dates, volumes, grades, monetary equivalent)
    - Petroleum or minerals taken by the SOE in-kind as coverage for a tax or other fiscal obligation (dates, volumes, grades, monetary equivalent)

- The sale proceeds from the sale of the SOE's production share, *as detailed in the note on in-kind revenues*
- Training fees, data fees
- Social contributions
- Payments for sale of shares of the SOE or of SOE shares in joint ventures

**Implementing this change:** Requirement 15 would need to be revised as below to indicate that revenues received by state-owned enterprises should be included along with government agency revenue disclosures: "Government agencies <u>(including state-owned companies)</u> comprehensively disclose all material revenues in accordance with the agreed reporting templates" [addition underlined].

B. **Reconciliation of material transfers made by the state-owned enterprise to the national treasury** or other unit of government (e.g. Finance Ministry or Central Bank). Depending on the type of SOE, these would include:
    - Transfers of revenues derived from the sale of state shares of oil or minerals
    - Transfers of other revenue streams collected by the NOC on behalf of the state
    - Income taxes
    - Dividend payments

**Implementing this change:** Requirement 11a of the EITI Rules states "The EITI Criteria require that all companies – public (state-owned) and private, foreign and domestic – report payments to the government, according to agreed templates, to the organisation appointed to reconcile disclosed figures." So, transfers between SOEs and the treasury already are mandatory, though compliance with this rule is very limited. Revision to the rule could clarify this requirement including the need for a reconciliation between the state and the treasury.

**A more robust reporting regime**, which could be a voluntary add-on, would include the public disclosure of the following elements:

- Annual reports and independent audits of state-owned enterprises
- Production volumes and reserves by license
- Equity holdings, sale and purchase of shares
- Detailed statement of costs, balance sheet
- Financial transfers among affiliated companies and subsidiaries within the umbrella of the SOE
- Detailed breakdown of expenditures for non-core activities, including social spending and other quasi-fiscal activity