IN THE MATTER OF GLOBAL WITNESS
AND IN THE MATTER OF
DRAFT INDUSTRY GUIDANCE
CONCERNING
THE REPORTS ON PAYMENTS TO GOVERNMENTS REGULATIONS 2014

OPINION

INTRODUCTION

1. I have been asked to advise on three questions set out in section 5 of my Instructions dated 11 February 2015. I will deal with each in turn, using the same abbreviations as those used in my Instructions and earlier in relation to the reporting obligation of undertakings under the Regulations and Directive 2013/34. I have split the first question on which I have been asked to advise into two.

QUESTION 1: is paragraph 5.2(iv) of the Guidance correct?

Opinion:

2. No.

Reasons:

3. I have been provided with a copy of the draft Guidance dated 5 November 2014 and a note of certain parts of the draft Guidance, as shown to those instructing me (and, I think, other CSO stakeholders) at an informal meeting on 6 February 2015. As I understand it, those at the meeting were not permitted to take away copies of the revised Guidance.

4. The point arising from paragraph 5.2(iv) of the Guidance on which I have been asked to advise is that, in the case of payments made to a state-owned enterprise acting as field operator, the Guidance states: "Disclosure is only required if the National Oil Company is paid one of the types of payment listed in Section 4 above *and if the amount of the reportable payment is distinguished from other costs"* (emphasis added).

5. The addition of the words in brackets is not mandated by either the 2014 Regulations or the Directive.

6. Paragraph 5.2(iv) is particularly troubling because it conveys the clear meaning that reportable payments are not subject to the disclosure obligation if they are rolled up into "other costs"; and it can therefore be construed as a discreet indicator as to how (in the view of the authors of the Guidance) the 2014 Regulations may be circumvented.

7. For the sake of clarity on this point, a reportable payment is (in short) an amount that is: (i) paid "for" relevant activities; and (ii) within one of a number of specified "types" of payment: see the definition in regulation 2(1). If both parts of the definition are satisfied, the payment is a reportable payment irrespective of whether or not it is "distinguished from other costs" (whatever that is supposed to mean).

QUESTION 2: is paragraph 7(ii) of the Guidance correct?

Opinion:

8. No, it is inaccurate.

Reasons:

9. Paragraph 7(ii) of the Guidance concerns the application of the reporting obligation to joint ventures. The particular question arising from paragraph 7(ii) on which I have been asked to advise concerns the suggestion that so-called "non-operating" parties to a joint venture agreement should not ("generally") report payments made by the joint

venture or by another party to the joint venture ("e.g. the operator") on behalf of the whole venture.

10. That approach is stated to reduce the risks of double counting, of creating uncertainty concerning the proportion of the payment to be included in each reporting entity's report and of inconsistent approaches being taken "between different joint ventures".

11. Why the recommended approach would reduce or obviate any of those risks is not apparent. For example, one would have supposed that a joint venturer making a payment into the joint venture, for the purpose of funding a reportable payment made by or on behalf of the joint venture, would know how much it had paid or would be able to obtain that information as of right from the joint venture. On the fact of it, it should be able to report the payment that it had made without running any of the risks referred to in the Guidance.

12. In any event, I cannot find in the 2014 Regulations and the Directive any legal basis for such guidance.

13. The expression "joint venture" covers a broad range of different structures that might be adopted by persons wishing to undertake a particular economic activity in conjunction with other persons.

14. The Directive applies to "undertakings" that take one of the forms (or "types") specified in Annexes I or II: see Article 1(1). Under the Directive, the reporting obligation applies to undertakings who are "active" in specified industries: see Articles 41(1) and (2), 42(1) and 44(1).

15. A joint venture could itself be an "undertaking" having one of the forms specified in Annexes I or II or one or more of the joint venturers could be such an undertaking.

16. If a joint venturer takes one of the forms specified in Annexes I or II, the reporting obligation applies to it if it is "active" in the industry concerned.

17. In the case of a joint venture that is "active" in any one of those industries, a party to the joint venture would normally be regarded as itself "active" in the industry in question by virtue of its participation in the joint venture. Arguably, that would not be the case if the joint venturer were a passive *minority* investor. By that expression, I mean a purely financial investor in the joint venture who plays no part in the direction or management of the joint venture and contributes no expertise to it. The possession of some role in the direction and management of the joint venture (such as through voting rights) would (in my view) make such a person an active participant in the joint venture and, through the joint venture, "active" in the industry in question. That is so irrespective of the size of the person's financial interest in the joint venture. A passive investor in the joint venture could not (in my view) avoid being regarded as "active" in that sense if it had a majority interest in the joint venture because, in the ordinary course, that would necessarily entail control of the joint venture and therefore some role in the direction and management of it.

18. The next point to note is that, by implication, the reporting obligation applies to payments made "by" the undertaking in question: see Article 43(2) (last sentence) (the Directive usually refers to payments made "to" governments without being specific about the person "by" whom they are made). However, there is no basis for believing that the reporting obligation applies only where the payment is made directly (as opposed to indirectly) to the government concerned: Article 43(4) provides that disclosure should reflect "the substance, rather than the form".

19. The upshot is that it is incorrect to say that so-called "non-operating parties" should "generally not include" in their reports the payment made by them to the operator.

20. In my view, paragraph 7(ii) is highly unsatisfactory in its treatment of joint ventures, to the extent of being positively misleading. I do think that giving guidance on joint ventures would be useful. The problem is that the authors of the Guidance have not explained that their views might be appropriate in relation to some types of joint venture arrangement but will not be appropriate for others.

21. The Guidance really starts to go wrong with the statement: "The duty to include a government payment in a report, and the determination of the amount to be included,

should be based on the payment arrangement that exists between the payer and the government, not by the cost sharing arrangement that exists between the parties to the joint venture".

22. It seems to me that the position is actually the reverse: it is necessary to start with an analysis of the joint venture arrangement in question, including the cost sharing aspect.

QUESTION 3: would the proposals set out in section 3.b of my Instructions reflect companies' obligations under the Regulations?

Opinion:

23. Broadly, yes, subject to some qualifications.

Reasons:

24. There are two alternative formulations in section 3.b of my Instructions. The first seems to me to be fairly accurate. The second, I think, tries to get to an acceptable result that is consistent with the policy behind the legislation; but it is not in full compliance with it.

25. The first formulation is as follows:

- Companies with obligations under the UK Regulations must disclose in-scope payments made on their behalf, whether by an operator or another agent.

- Where a payment duty is paid by an operator on behalf of participants in the joint venture, participating companies should disclose their share of the relevant payment.

- In determining whether a payment has been made on a company's behalf (as opposed to by an operator acting as principal), companies should have regard to the underlying liability for the payment under local taxation law and whether this is a payment which the company would be required to include in its financial statements under relevant accounting rules.

26. I think that that formulation would work as appropriate guidance but, if it was thought desirable to go into the kind of detail that one finds in paragraph 7(ii) of the Guidance,

it would be necessary to give some further thought to the problems posed by joint ventures.

QUESTION 4: what are the implications for the UK Government if a version of the Guidance were adopted as per the revised wording?

Opinion:

27. In my view, it would be inappropriate for BIS to endorse the Guidance.

Reasons:

28. In my view, the Guidance is inaccurate and misleading. In those circumstances, it would be unwise and inappropriate for the Guidance to be endorsed by BIS. If the Guidance remains as something that has been drawn up by industry and has not received the benediction of BIS, there is no commitment by the UK Government to the errors contained in the Guidance. That means that the Guidance does not, in itself, expose the UK to infringement proceedings and should not have any effect on BIS' ability to prosecute breaches of the Regulations. The position would be different if the Guidance were endorsed by BIS.

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