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Resource Extraction Payments Disclosure Rules Redux – The SEC Proposes New Rules

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On December 18, 2019, the SEC proposed a new Rule 13q-1 under the Exchange Act and related amendments to Form SD. The Proposed Rules would require public companies to annually report on payments made to foreign governments and the U.S. Federal government relating to the commercial development of oil, natural gas and minerals.

Section 1504 of the Dodd-Frank Act added Section 13(q) to the Exchange Act. Section 13(q) in turn directs the SEC to issue rules requiring resource extraction issuers to include in an annual report information relating to payments made to a foreign government or the U.S. Federal government for the purpose of the commercial development of oil, natural gas or minerals. The intent of Section 1504 is to help combat global corruption and empower citizens of resource-rich countries to hold their governments accountable for the wealth generated by those resources, by making resource extraction payments more transparent.

The Proposed Rules are the SEC's third attempt at implementing this Dodd-Frank mandate. The Proposed Rules address many of the concerns raised on the previous attempts, and would result in regulation that is overall less burdensome for issuers. This Alert describes the Proposed Rules, including how they differ from the rules adopted by the SEC in 2016.

The Curious History of Rule 13q-1

The current rule-making proposal is the SEC's third bite at the apple. Resource extraction payments transparency rules were first adopted by the SEC during August 2012, but were subsequently challenged in court – like some other Dodd-Frank rulemaking initiatives – and then vacated by the U.S. District Court for the District of Columbia during July 2013. The District Court vacated the 2012 Rules on two grounds. First, the District Court concluded that the SEC misread the statute to require the public filing of the payments disclosure to be made by issuers. Second, it concluded that the SEC's failure to include an exemption in the 2012 Rules for countries that prohibit payments disclosure was "arbitrary and capricious" within the meaning of the Administrative Procedure Act.

Unhappy that the SEC had not yet re-proposed resource extraction payments disclosure rules, during September 2014, Oxfam America filed suit to compel the SEC to adopt new rules. During September 2015, the U.S. District Court for the District of Massachusetts concluded that the SEC's delay in re-promulgating resource extraction payments disclosure rules amounted to final agency action "unlawfully withheld" under the Administrative Procedure Act and ordered the SEC to file an expedited schedule with its plans to finalize the rules. A second, revised Rule 13q-1, and corresponding amendments to Form SD, were adopted during June 2016.

The 2016 Rules were subsequently disapproved during February 2017, pursuant to the Congressional Review Act, by a joint Congressional resolution, which was then signed by the President. Under the CRA, Congress may disapprove a broad range of federal regulatory rules (within a certain specified period after a rule has been submitted to Congress) by adopting a joint resolution of disapproval, which, once enacted into law, prevents the rule from taking or continuing in effect. Concerns of members of Congress who supported the joint resolution included the potential adverse economic effects of the 2016 Rules due to the compliance costs that subject companies would incur and competitive harm relative to foreign companies not subject to similar requirements.

Under the CRA, a federal agency is barred from reissuing a new rule in substantially the same form as the disapproved rule, unless the new rule is specifically authorized by a law enacted after the date of the joint resolution disapproving the original rule. The Proposed Rules differ from the 2016 Rules in several significant respects. In developing the Proposed Rules, among other things, the SEC looked to the concerns raised by members of Congress during the floor debates on the joint resolution.

As additional context, for further information on the 2016 Rules, see our earlier Alerts here and here. In addition, our comment letter on the 2016 Rules is available here. We were one of the few law firms that submitted comments on the 2016 Rules and were pleased that some of our comments made their way into the final 2016 Rules (and in turn the Proposed Rules).

What's New in the Proposed Rules? – A High-Level Overview

As discussed in more detail in this Alert, the Proposed Rules contain several significant changes from the 2016 Rules. The Proposed Rules:

- Revise the definition of "project" to require disclosure at the national and major subnational political jurisdiction, as opposed to the contract, level;
- Revise the definition of "not de minimis" to include both a project threshold and an individual payment threshold;
- Add two new conditional exemptions for situations in which a foreign law or a pre-existing contract prohibits required disclosure;
- Add an exemption for smaller reporting companies and emerging growth companies;
- Revise the definition of "control" to exclude entities or operations in which an issuer has a proportionate interest;
- Limit the liability for required disclosure by deeming payment information to be furnished to, but not filed with, the SEC;
- Permit an issuer to aggregate payments by payment type made at a level below the major subnational government level;
- Add relief for issuers that have recently completed their U.S. IPOs; and
- Extend the deadline for furnishing disclosures.

Issuers Coming Under the Proposed Rules

"Resource extraction issuers" would have disclosure obligations under the Proposed Rules. This term would include all issuers that:

- file annual reports on Form 10-K, Form 20-F or Form 40-F; and
- are engaged in the commercial development of oil, natural gas or minerals.

In contrast to the 2016 Rules, emerging growth companies and smaller reporting companies would not be subject to the Proposed Rules.

Consistent with the 2016 Rules, registered investment companies, Rule 12g3-2(b) issuers and issuers subject to Tier 2 reporting obligations under Regulation A would be outside the scope of the Proposed Rules.

The SEC estimates that approximately 345 issuers would be subject to the Rules as proposed. According to the Proposing Release, 109 of these issuers are likely to be able to avail themselves of alternative reporting provisions as contemplated by the Proposed Rules, since they have a business address, are incorporated in or listed on markets in the

European Economic Area or Canada and are therefore assumed by the SEC to already publish more granular resource extraction payments disclosure. Two EU directives – the EU Accounting Directive and the EU Transparency Directive – contain payments disclosure requirements similar to the 2016 Rules. Canada has adopted the Extractive Sector Transparency Measures Act, which also is similar to the 2016 Rules.

Applicability to Controlled Entities and Subsidiaries. Under the Proposed Rules, a resource extraction issuer would also be required to disclose payments made by its subsidiaries and other entities under its control. Consistent with the 2016 Rules, whether an entity is a "subsidiary" or there is "control" is based on accounting principles, rather than having the meaning contained in Rule 12b-2 of the Exchange Act.

Under the Proposed Rules, a "subsidiary" is defined as an entity controlled directly or indirectly through one or more intermediaries.

A resource extraction issuer would have "control" of another entity if the issuer consolidates that entity under the accounting principles applicable to the U.S. GAAP or IFRS financial statements included in its Exchange Act reports. A foreign private issuer that prepares financial statements according to a comprehensive set of accounting principles other than U.S. GAAP or IFRS and that files a U.S. GAAP reconciliation would be required to determine control using U.S. GAAP. In a departure from the 2016 Rules, the Proposed Rules would exclude from the definition of "control" an interest in an entity or operation that is proportionately consolidated by the issuer. Proportionately consolidated entities or operations include those entities or operations that are proportionately consolidated in accordance with ASC 810-10-45-14 and "joint operations" as defined in IFRS 11, Joint Arrangements.

Covered Activities

The activities that come within the scope of the Proposed Rules are the commercial development of oil, natural gas or minerals.

The Proposed Rules do not define the terms "oil," "natural gas" or "minerals." In the case of minerals, the SEC indicates that it believes that term is commonly understood. The Proposed Rules, however, include an Instruction indicating that "minerals" includes any material for which an issuer with mining operations would provide disclosure under the SEC's current disclosure requirements and policies, including Industry Guide 7. Industry Guide 7 requires specified information relating to the properties of issuers engaged or to be engaged in significant mining operations.

"Commercial Development of Oil, Natural Gas or Minerals" Defined. The Proposed Rules define this term to include the exploration, extraction, processing and export of oil, natural gas or minerals, or the acquisition of a license for any of the foregoing activities. This definition is consistent with the 2016 Rules.

The Proposing Release notes that commercial development would capture only activities that are directly related to the commercial development of oil, natural gas or minerals. The Proposing Release indicates that the SEC would not consider ancillary or preparatory services to be within the scope of the Proposed Rules. This would exclude, for example, an issuer that manufactures drill bits or provides hardware to help companies to explore or extract. Similarly, an issuer engaged by an operator to provide hydraulic fracturing or drilling services would not be considered a resource extraction issuer. Marketing activities and security support also would not be included.

Meanings of "Extraction," "Export" and "Processing." To help clarify which activities come within "commercial development," the Proposed Rules define and/or provide guidance on the meanings of the terms "extraction," "export" and "processing." These are consistent with the 2016 Rules.

- ***Extraction.*** The production of oil and natural gas as well as the extraction of minerals.
- ***Export.*** The movement of a resource across an international border from the host country to another country by a company with an ownership interest in the resource.

Cross-border transportation activities by an issuer that is functioning solely as a service provider on a fee-for-service basis, with no ownership interest in the resource being transported, would not considered to be an export.

"Export" also is not intended to capture activities with little relationship to upstream or midstream activities, such as commodity trading-related activities.

However, the Proposing Release indicates that "export" would cover the purchase of government-owned resources by an issuer otherwise engaged in resource extraction, due to the stronger nexus between the movement of the resource across an international border and the upstream development activities. The Proposing Release indicates that this link would be particularly strong in instances where the issuer is repurchasing government production entitlements that it originally extracted.

- ***Processing.*** The Instructions to the Proposed Rules provide examples of activities that would constitute processing.

  Instruction (8) indicates that processing would include, but not be limited to, midstream activities such as removing liquid hydrocarbons from gas, the removal of impurities from natural gas prior to its transport through a pipeline and upgrading bitumen and heavy oil, through the earlier of the point at which oil, gas or gas liquids (natural or synthetic) are either sold to an unrelated third party or delivered to a main pipeline, a common carrier or a marine terminal.

  Processing also would include the crushing or preparing of raw ore prior to the smelting phase, but not the downstream activities of refining or smelting (since issuers do not typically make payments to host governments in connection with refining or smelting).

Anti-Evasion Provision. The Proposed Rules include an anti-evasion provision that would require disclosure concerning an activity, payment or series of payments that, although not within one of the categories of activities or payments specified in the Proposed Rules, is part of a plan or scheme to evade the Proposed Rules. The Proposing Release notes that this provision would cover, for example, payments that were substituted for otherwise reportable payments in an attempt to evade the disclosure requirements of the Proposed Rules, as well as activities and payments that were structured, split or aggregated in an attempt to avoid application of the Proposed Rules. The Proposing Release notes that, similarly, a resource extraction issuer could not avoid disclosure by re-characterizing an activity as transportation that would otherwise be covered under the Proposed Rules, or by making a payment to the government via a third party in order to avoid disclosure under the Proposed Rules.

Definitions of "Foreign Government" and "Federal Government"

Consistent with the 2016 Rules, the Proposed Rules only would require disclosure of payments to a foreign government or the U.S. Federal government.

The Proposed Rules define "foreign government" broadly. In addition to a national foreign government, the Proposed Rules includes within the definition:

- a department, agency or instrumentality of a foreign government;
- a company at least majority-owned by a foreign government; and
- a foreign subnational government, such as the government of a state, province, county, district, municipality or territory under a foreign national government.

"Federal government" would mean the U.S. Federal government. Payments made to U.S. state, local or other subnational governments would not be required to be disclosed, since disclosure of these payments is not contemplated by Section 13(q).

Payments Within (and Outside) the Scope of the Proposed Rules

Under the Proposed Rules, a resource extraction issuer would be required to disclose specified types of payments that are made to further the commercial development of oil, natural gas or minerals.

"Payment" Defined. The definition of "payment" would include the following:

- Taxes.

  Payments made for taxes on corporate profits, corporate income and production would be required to be disclosed. However, payments made for taxes levied on consumption, such as value-added taxes, personal income taxes or sales taxes would not be required to be disclosed. (Instruction (9)) As discussed later in this Alert, payments for obligations levied at the enterprise level, such as corporate taxes, would be able to be disclosed at the entity level, rather than the project level.

- Royalties.

  Royalties would include, but not be limited to, unit-based, value-based and profit-based royalties. (Instruction (10))

- Fees.

  Fees would include, but not be limited to, license fees, rental fees, entry fees and other consideration for licenses or concessions. (Instruction (9))

- Production entitlements.

- Bonuses.

  Bonuses would include, but not be limited to, signature, discovery and production bonuses. (Instruction (10))

- Dividends.

  Dividends paid to a government as a common or ordinary shareholder of the resource extraction issuer that are paid under the same terms as to other shareholders would not be required to be disclosed. However, any dividends paid in lieu of production entitlements or royalties would be required to be disclosed. (Instruction (11))

- Payments for infrastructure improvements.

  Examples cited in the Proposing Release include payments for building a road or railway to further the development of oil, natural gas or minerals.

- Community and social responsibility payments required by law or contract.

  Examples cited in the Proposing Release include funds to build or operate a training facility for oil and gas workers, funds to build housing, payments for tuition or other educational purposes, and, in general, payments to support the social or economic well-being of communities within the country where the expenditures are made.

In-Kind Payments. Pursuant to Instruction (12), if an in-kind payment of a type of payment required to be disclosed is made, the in-kind payment would be required to be disclosed. The Proposing Release cites as examples production entitlement payments and infrastructure payments.

Excluded Payments. Consistent with the 2016 Rules, the Proposing Release indicates that the following would not be within the scope of the Proposed Rules: (1) commodity trading-related payments (other than in-kind production entitlement payments); (2) payments for government expenses, providing jobs or tuition to persons related to government officials, investing in companies created by officials or related persons, or other similar payments (although the Proposing Release notes that, when these payments are made to further the commercial development of oil, natural gas or minerals, they would be covered by the anti-evasion provision of the Proposed Rules); and (3) fines and penalties.

De Minimis Threshold. Only payments that are "not de minimis" would be required to be disclosed.

The Proposed Rules increase the de minimis threshold from the 2016 Rules and bifurcate the threshold into two components. Under the 2016 Rules, a payment would be de minimis if it is a single payment or series of related payments that is less than $100,000 (or its equivalent in the issuer's reporting currency) during the fiscal year covered by the filing. Under the Proposed Rules, an issuer would not be required to provide disclosure if the aggregate project payments for all types of payments for an individual project are below $750,000. If the aggregate payments for an individual project equal or exceed $750,000, only payments made to each foreign government in a host country or the Federal government that equal or exceed $150,000, or its equivalent in the issuer's reporting currency, whether made as a single payment or a series of related payments, would need to be reported.

If an arrangement provides for periodic payments or installments, the resource extraction issuer would be required to use the aggregate amount of the related periodic payments or installments of the related payments in determining whether the payment threshold has been met for that series of payments and disclosure is required.

Instruction (2) to the Proposed Rules indicates that, when calculating whether the de minimis threshold has been exceeded for purposes of reporting a payment, a resource extraction issuer may be required to convert the payment to U.S. dollars, even though it would not be required to disclose those payments in U.S. dollars. The Instruction indicates that, for example, this may occur when the resource extraction issuer is using a non-U.S. dollar reporting currency. There are three methods that would be able to be used for calculating currency conversions, as described later in this Alert.

Payments Made Through Service Providers. Instruction (7) provides that, if a service provider makes a payment that falls within the definition of "payment" to a government on behalf of a resource extraction issuer, the resource extraction issuer would be required to disclose the payment.

Definition of "Project"

Section 13(q) requires resource extraction issuers to provide information about the type and total amount of payments made for each of their projects related to the commercial development of oil, natural gas or minerals.

The Proposed Rules define "project" differently than the 2016 Rules. In the Instructions to the Proposed Rules, "project" is defined by using the three criteria described below. In contrast, the 2016 Rules contained a contract-based definition of "project," which was defined as the operational activities governed by a single contract, license, lease, concession or similar legal agreement, which form the basis for payment liabilities with a government. Notably, the SEC had considered, but rejected, the currently proposed definition of "project" as part of the 2016 rule-making process.

Under the Proposed Rules, "project" is defined using the following criteria:

- The type of resource being commercially developed.

  As proposed in new Instruction (5)(i), a resource extraction issuer would have to disclose whether the project relates to the commercial development of oil, natural gas or a specified type of mineral. The proposed Instruction indicates that a resource extraction issuer should identify synthetic oil obtained through processing tar sands, bitumen or oil shales as "oil" and should identify gas obtained from methane hydrates as "natural gas." Synthetic oil or gas obtained through processing of coal should be identified as "coal." Minerals would be required to be identified by type, such as gold, copper, coal, sand or gravel, but additional detail would not be required.

The Proposing Release notes that a resource extraction issuer would not be required to describe the specific type or quality of oil or natural gas or distinguish between subcategories of the same mineral type. For example, an issuer disclosing payments relating to an oil project would not be required to describe whether it is extracting light or heavy crude oil. Similarly, an issuer disclosing payments relating to a mining project would be required to disclose whether the mineral is gold, copper, coal, sand, gravel or some other generic mineral class, but not whether it is, for example, bituminous coal or anthracite coal.

- The method of extraction.

  As indicated in Instruction (5)(ii), a resource extraction issuer would be required to identify whether the resource is being extracted through the use of a well, an open pit or underground mining. According to the Proposing Release, additional detail about the method of extraction would not be required. For example, a resource extraction issuer would not be required to disclose whether it is using horizontal or vertical drilling, hydraulic fracturing, or strip, sublevel stope or block cave mining.

- The major subnational political jurisdiction where the commercial development of the resource is taking place.

  The issuer would be required to disclose only two levels of jurisdiction: (1) the country; and (2) the state, province, territory or other major subnational jurisdiction in which the resource extraction activities are occurring.

  Under Instruction (5)(iv), a resource extraction issuer would be permitted to treat all the activities within a major subnational political jurisdiction as a single project, although it would be required to describe each type of resource being commercially developed and each method of extraction used in the description of the project. A resource extraction issuer would not be able to combine as one project activities that cross the borders of a major subnational political jurisdiction.

  Proposed Instruction (5)(iii) indicates that onshore and offshore development of resources would not be able to be treated as a single project. A resource extraction issuer would be required to identify when a project is offshore and identify the nearest major subnational political jurisdiction.

Information to Be Reported

Under the Proposed Rules, the information indicated below would be required to be provided. The categories of information to be provided are largely the same as under the 2016 Rules. However, due to changes to the definition of "project," changes to payment thresholds, the ability to aggregate payments made below the major subnational government level by payment type, the addition of new conditional exemptions and the other proposed rule changes discussed in this Alert, the disclosures that would be required are somewhat different than under the 2016 Rules.

Selected project-specific disclosures are described in the discussion of the definition of "project" earlier in this Alert, rather than in this portion of the Alert. The payment categories for which disclosure would be required also are discussed earlier in this Alert.

- The type and total amount of the payments, by payment type, made for each project of the resource extraction issuer relating to the commercial development of oil, natural gas or minerals.
- The type and total amount of the payments, by payment type, for all projects made to each government.
- The total amounts of the payments, by payment type.
- The currency used to make the payments.
- The fiscal year in which the payments were made.
- The business segment of the resource extraction issuer that made the payments.

For purposes of the Proposed Rules, a business segment is consistent with the reportable segments used by the resource extraction issuer for purposes of financial reporting.

- The governments that received the payments, and the country in which each such government is located.

  For payments made at the major subnational government level, the issuer would have to disclose the particular major subnational payee, although it could aggregate all of its payments of a particular payment type.

  For purposes of identifying the foreign governments that received payments at a level below the major subnational government level, the Proposed Rules would permit an issuer to aggregate all of its payments of a particular payment type without having to identify the particular subnational government payee. The issuer would only be required to identify the type of administrative or political level of subnational government that received the payments. For example, an issuer could aggregate payments by payment type made to multiple counties and municipalities (the level below major subnational government level) and disclose the aggregate amount without having to identify the particular subnational government payee.

- The project of the resource extraction issuer to which the payments relate.

- The particular resource that is the subject of commercial development.

- The method of extraction used in the project.

  This item was not part of the 2016 Rules. The manner in which the method of extraction would be required to be described is discussed earlier in this Alert.

- The major subnational political jurisdiction of the project.

  This item was modified in the Proposed Rules relative to the 2016 Rules, to reflect the proposed change to permit an issuer to treat all the activities within a major subnational jurisdiction as a single project.

Entity Level Payments. Consistent with the 2016 Rules, the Proposed Rules include a clarifying instruction (Instruction (4)) indicating that resource extraction issuers would not need to disaggregate payments that are made for obligations levied on the issuer at the entity level rather than the project level.

Calculating Payments; Audits

Cash Basis. Payment information would be required to be provided on a cash basis.

Reporting Currency; Currency Conversions. Payments would be required to be reported in either U.S. dollars or the resource extraction issuer's reporting currency if not U.S. dollars. If payments were made in a currency other than its reporting currency or U.S. dollars, the issuer would be permitted to choose to calculate the currency conversion in one of three ways:

- by translating the expenses at the exchange rate at the time the payment is made;

- using a weighted average of the exchange rates during the period; or

- based on an exchange rate as of the issuer's fiscal year end.

The method used to calculate the currency conversion must be disclosed. In addition, a consistent method must be used for all currency conversions within the same submission.

Proportionate Consolidation. If a resource extraction issuer proportionately consolidates an entity or operation under U.S. GAAP or IFRS and is required to disclose payments made by that entity under the Proposed Rules, the issuer would be required to disclose its proportionate amount of the payments made and to indicate its proportionate interest.

Valuing In-Kind Payments. Instruction (12) to the Proposed Rules indicates that, when reporting an in-kind payment, the resource extraction issuer would be required to determine the monetary value of the payment and tag the information as "in-kind" for purposes of the currency.

The issuer would be required to report the payment at cost, or, if cost is not determinable, fair market value, and must provide a brief description of how the monetary value was calculated. If a resource extraction issuer makes an in-kind production entitlement payment and then repurchases the resources associated with the production entitlement within the same fiscal year, the resource extraction issuer would be required to report the payment using the purchase price (rather than at cost, or, if cost is not determinable, fair market value). If the in-kind production entitlement payment and the subsequent repurchase are made in different fiscal years and the purchase price is greater than the previously reported value of the in-kind payment, the resource extraction issuer would be required to report the difference in values in the latter fiscal year (assuming the amount of that difference exceeds the de minimis threshold). In other situations, such as when the purchase price in a subsequent fiscal year is less than the in-kind value already reported, no disclosure relating to the purchase price would be required.

Audit Not Required. The Proposed Rules indicate that a resource extraction issuer would not be required to have the payment information presented in its Form SD audited. This is consistent with the 2016 Rules.

Transition and Other Exemptions

The Proposed Rules would add two new targeted exemptions addressing conflicts with laws and pre-existing contracts. The Proposed Rules also would add a new transition exemption for IPO issuers, in addition to the transition exemptions relating to exploratory activities and acquired companies carried over from the 2016 Rules. As discussed below, issuers also would be able to apply for exemptions on a case-by-case basis.

Consistent with the 2016 Rules, the Proposed Rules do not include blanket exemptions where disclosure would jeopardize competitively sensitive information or potentially jeopardize the safety and security of employees and operations. However, the SEC notes in the Proposing Release that it believes the changes being proposed should help to alleviate these concerns.

As noted earlier in this Alert, an exemption also would be added for emerging growth companies and smaller reporting companies.

Legal Conflicts. If a resource extraction issuer is prohibited by the law of the jurisdiction where the project is located from providing the payment information required by Form SD, it would be permitted to exclude that disclosure, subject to the following conditions:

- The issuer took all reasonable steps to seek and use any exemptions or other relief under the applicable law of the foreign jurisdiction, and was unable to obtain or use such an exemption or other relief;
- The issuer discloses on Form SD the foreign jurisdiction for which it is omitting the disclosure, the particular law of that jurisdiction that prevents the issuer from providing the disclosure and the efforts the issuer undertook to seek and use exemptions or other relief under the applicable law of that jurisdiction, and the results of those efforts; and
- The issuer furnishes as an exhibit to Form SD a legal opinion from counsel that opines on the issuer's inability to provide such disclosure without violating the foreign jurisdiction's law.

As proposed, the exemption would not be limited to pre-existing foreign laws.

Contractual Conflicts. A resource extraction issuer that is unable to provide the payment information required by Form SD without violating one or more contract terms that were in effect prior to the effective date of the Proposed Rules would be permitted to exclude that disclosure, subject to the following conditions:

- The issuer took all reasonable steps to obtain the consent of the relevant contractual parties, or to seek and use another contractual exception or relief, to disclose the payment information, and was unable to obtain such consent or other contractual exception or relief;
- The issuer discloses on Form SD the jurisdiction for which it is omitting the disclosure, the particular contract terms that prohibit the issuer from providing the disclosure and the efforts the issuer undertook to obtain the consent of the contracting parties, or to seek and use another contractual exception or relief, to disclose the payment information, and the results of those efforts; and
- The issuer furnishes as an exhibit to Form SD a legal opinion from counsel that opines on the issuer's inability to provide such disclosure without violating the contractual terms.

Payments Relating to Exploratory Activities. Consistent with the 2016 Rules, the Proposed Rules include a temporary exemption for payments relating to exploratory activities. Resource extraction issuers would be permitted to delay reporting these payments until the fiscal year following the fiscal year in which the payments were made.

Payments would be considered to be related to exploratory activities if they are made as part of (1) the process of identifying areas that may warrant examination, (2) the process of examining specific areas that are considered to have prospects of containing oil and gas reserves or (3) a mineral exploration program. However, exploratory activities are limited to activities commenced prior to commercial development (other than exploration) on the property, any adjacent property or on any property that is part of the same project.

Acquired Entities. Also consistent with the 2016 Rules, under the Proposed Rules, a resource extraction issuer that acquires or otherwise obtains control over another entity that was not obligated in its last full fiscal year to provide disclosure pursuant to Rule 13q-1 or another alternative reporting regime recognized by the SEC, would not be required to commence reporting payment information for the acquired entity until the Form SD submission for the fiscal year immediately following the effective date of the acquisition. The resource extraction issuer would be required to disclose that it is relying on this accommodation in the body of its Form SD submission.

IPO Issuers. A resource extraction issuer that has completed its initial public offering in the United States in its last full fiscal year would not be required to commence reporting payment information pursuant to Rule 13q-1 until the Form SD submitted for the fiscal year immediately following the fiscal year in which the registration statement for its U.S. initial public offering became effective.

Case-by-Case Exemptions. To address any other potential bases for exemptive relief, the Proposed Rules provide that issuers could apply for exemptions on a case-by-case basis using the procedures set forth in Rule 0-12 of the Exchange Act. An issuer seeking an exemption would be required to submit a written request for exemptive relief to the SEC describing the particular payment disclosures that it seeks to omit and the specific facts and circumstances that it believes warrant an exemption, including the particular costs and burdens it faces if the information is disclosed.

The Proposing Release notes that, in situations where exigent circumstances exist, the SEC staff, acting pursuant to delegated authority, could rely on Exchange Act Section 12(h) for the limited purpose of providing interim relief while the SEC considered the exemptive application.

Form, Format and Other Submission Requirements

Submissions on Form SD. Disclosures would be required to be submitted on Form SD through the SEC's EDGAR system. This aspect of the Proposed Rules is further discussed below.

All of the substantive disclosure required to be submitted would be contained on an exhibit – Exhibit 2.01 – to the Form SD.

In a reversal from the 2016 Rules, the information provided by resource extraction issuers on Form SD would be "furnished" instead of "filed." The distinction is that furnished information is not subject to liability under Section 18 of the Exchange Act.

Although the SEC has again proposed a public disclosure regime, the Proposing Release indicates that, while the SEC preliminarily believes that the Proposed Rules strike an appropriate balance, it also is considering the alternative approach of permitting resource extraction issuers to submit their annual reports on Form SD to the SEC non-publicly. The SEC would then use the non-public submissions to produce an aggregated, anonymized public compilation. The SEC has asked for commenters' views on this aspect of the Proposed Rules.

Submission Due Dates; Initial Compliance Date. Under the 2016 Rules, filings would have been required no later than 150 days after the end of the applicable fiscal year. In the Proposed Rules, the SEC is proposing a longer submission deadline. As proposed, an issuer with a fiscal year ending on or before June 30 would be required to submit its Form SD no later than March 31 in the calendar year following its most recent fiscal year. For an issuer with a fiscal year ending after June 30, the Form SD submission deadline would be no later than March 31 in the second calendar year following its most recent fiscal year.

The Proposed Rules would require a resource extraction issuer to comply with the Rules for fiscal years ending no earlier than two years after their effective date. The proposed two-year transition period is the same as the transition period in the 2016 Rules. The SEC also is proposing to select a specific compliance date that corresponds to the end of the nearest calendar quarter following the effective date.

XBRL Requirements. Payment disclosure required by the Proposed Rules would be required to be presented in the eXtensible Business Reporting Language (XBRL) electronic format and contain XBRL tags. The tags would consist of both tags with fixed definitions and customizable tags.

A resource extraction issuer would be permitted to omit data tags that are inapplicable because the payments relate to obligations levied at the entity level. Examples of tags that might be omitted are the project tag and business segment tag. The resource extraction issuer would be required to provide all other electronic tags, including the tag identifying the recipient government.

Location Tagging. Proposed Instruction (3) indicates that, when identifying the country and major subnational political jurisdiction where the commercial development of the resource is taking place, a resource extraction issuer would be required to use the combined country and subdivision code provided in ISO 3166, if available. When identifying the country in which a government is located, a resource extraction issuer would be required to use the two letter country code provided in ISO 3166, if available.

Inline XBRL Not Required. The Proposing Release indicates that Inline XBRL would not be required. Inline XBRL is a format that allows filers to embed XBRL data directly into an HTML document. Given the nature of the disclosure required by the Proposed Rules, which is primarily an exhibit with tabular data, the SEC has indicated that it does not believe that Inline XBRL would improve the usefulness or presentation of the required disclosure.

Subsidiary and Other Controlled Entity Registrants. If a resource extraction issuer is controlled by another resource extraction issuer that has submitted a Form SD disclosing the information otherwise required to be disclosed by the controlled entity, then the controlled entity would not be required to separately provide the same disclosure. The

controlled entity only would be required to submit a notice on Form SD indicating that the disclosure was submitted by the controlling entity, identifying the controlling entity and the date the information was submitted. The reporting controlling entity also would be required to note that it is submitting the disclosure for the controlled entity and to identify the controlled entity in its submission.

Alternative Reporting

The Proposed Rules contemplate allowing issuers to submit disclosures made pursuant to foreign resource extraction payments disclosure regulations. The SEC proposed a similar approach in connection with the 2016 Rules.

Substantive Reporting Requirements. Under the Proposed Rules, a resource extraction issuer that is subject to the payments disclosure requirements of an alternative reporting regime that has been deemed by the SEC to require disclosure that satisfies the transparency objectives of Section 13(q) may meet its Form SD disclosure obligations by including as an exhibit to its Form SD a report complying with the reporting requirements of the alternative jurisdiction.

The alternative report would be required to be the same as that which is prepared and made publicly available pursuant to the requirements of the approved alternative reporting regime.

Additional Form SD Disclosures. The resource extraction issuer would be required to (1) state in the body of the Form SD that it is relying on the alternative reporting provision; (2) identify the alternative reporting regime for which the report was prepared; (3) describe how to access the publicly submitted report in the alternative jurisdiction; and (4) specify that the payment disclosure required by Form SD is included in an exhibit to the Form.

XBRL. The alternative report would be required to be provided in XBRL format.

Translations. A fair and accurate English translation of the entire report would be required to be submitted if the report is in a foreign language.

Timing. The resource extraction issuer would be permitted to follow the submission deadline of the approved alternative jurisdiction if it submits a notice on Form SD-N on or before the due date of its Form SD indicating its intent to submit the alternative report using the alternative jurisdiction's deadline. If a resource extraction issuer fails to submit the notice on a timely basis, or submits a notice but fails to submit the alternative report within four business days of the alternative jurisdiction's deadline, it would not be able to rely on the alternative reporting accommodation for the following fiscal year.

Additional Requirements. Resource extraction issuers also would be required to comply with any additional requirements that are provided by the SEC in connection with permitting alternative reporting.

Designation of Alternative Reporting Regimes. The Proposing Release indicates that the SEC anticipates making determinations as to whether a foreign jurisdiction's disclosure requirements satisfy Section 13(q)'s transparency objectives either on its own initiative or pursuant to an application submitted by an issuer or a jurisdiction. The SEC indicated in the Proposing Release that it would anticipate considering the following criteria, among others:

- the types of activities that trigger disclosure;
- the types of payments that are required to be disclosed; and
- whether project-level disclosure is required and, if so, the definition of "project."

Pursuant to a separate Order issued on the same day as the 2016 Rules, the SEC determined that the EU Accounting Directive and Transparency Directive, Canada's Extractive Sector Transparency Measures Act and the U.S. Extractive Industries Transparency Initiative were substantially similar to the 2016 Rules. That Order is described in more detail in our earlier Alert.

Next Steps in the Rule-making Process

The Proposed Rules are in the comment phase. The comment period is open until 60 days after the Proposed Rules are published in the Federal Register. That had not yet occurred when this Alert was released. In the Proposing Release, the SEC requested feedback on 86 specific questions, although comments may be submitted on other aspects of the Proposed Rules as well. Prior to adoption, the Proposed Rules may therefore undergo further – possibly significant – changes.

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