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SEC Adopts Final Disclosure Rules for Resource Extraction Issuers

On December 16, 2020, the SEC adopted final disclosure rules (available [here](#)) that will require resource extraction issuers to disclose payments made to the U.S. federal government or foreign governments for the commercial development of oil, natural gas or minerals. The rule applies to SEC-reporting domestic issuers as well as foreign private issuers. The final rules seek to address the concerns highlighted in prior versions of the rules.¹

The SEC simultaneously issued an order (available [here](#)) permitting issuers (domestic and foreign private issuers) to provide, in lieu of disclosure mandated by the final rules, resource extraction payment disclosures already required of them under: (i) Canada's Extractive Sector Transparency Measures (ESTMA); (ii) the EU Accounting Directive 2013/34/EU; (iii) the EU Transparency Directive 2013/50/EU; (iv) the UK Reports on Payment to Governments Regulation 2014; or (v) the Norwegian Regulation on Country-by-Country Reporting.

Key highlights of the final rules:

- issuers must present payments by type and total amount per project on Form SD;
- payments must be reported at national and “major subnational” political jurisdiction levels (under the definition of “project,” which is a change from the previously proposed 2016 definition which would have required presentation instead at the contract level);
- disclosure will only be required if the total aggregate payments for a project exceed \$100,000 (under the definition of “not de minimis,” consistent with the 2016 proposal);
- issuers must disclose payments made to subsidiaries and entities controlled by the issuer, though issuers need not disclose payments made by entities that are only proportionally consolidated by the issuer (under the definition of the term “control,” a revision from the 2016 proposal);
- issuers may aggregate these payments by type at the major subnational jurisdiction level, but must disclose an aggregated amount for each subnational government payee and identify each subnational government payee;

¹ For summary of the 2016 resource extraction payment disclosure rules, see our July 2016 client alert entitled “[SEC Adopts Disclosure Rules for Resource Extraction Issuers](#).”

- certain smaller reporting companies and emerging growth companies will be eligible for exemptions, as will issuers that are subject to foreign law in situations where foreign law or preexisting contractual terms prohibit the disclosure;
- disclosure on Form SD will be deemed *furnished* to, as opposed to being *filed* with, the SEC; and
- there is an extended deadline for providing the disclosures as well as IPO transitional relief.

The final rules will become effective 60 days after the date of publication in the *Federal Register*.

Background

Section 1504 of the Dodd-Frank Act of 2010 directed the SEC to issue rules requiring resource extraction issuers to include, in an annual report, information relating to any payment made by the issuer or its affiliates to the U.S. federal government or a foreign government for the purpose of the commercial development of oil, natural gas or minerals. The original resource extraction rule was adopted by the SEC in August 2012. Following a challenge by the American Petroleum Institute, the U.S. Chamber of Commerce and two other industry groups in 2013, the rule was vacated by the U.S. District Court for the District of Columbia.

In December 2015, the SEC re-proposed the resource extraction disclosure rule. The rule was adopted in June 2016 and would have required that resource extraction issuers comply with the disclosure requirements starting with their fiscal year ending on or after September 30, 2018. However, before the rule came into effect, in February 2017, Congress passed a resolution under the Congressional Review Act (“CRA”) eliminating the rule and instructing that any future rules on extraction payments disclosure may not be “substantially the same” or in “substantially the same format” as the disapproved rules.

In December 2019, the SEC, for the third time, published revised rule proposals for the resource extraction payments disclosure, which were finally adopted with some amendments on December 16, 2020.

Final Rules

Applicability

The final rules apply to resource extraction issuers, which includes issuers that are required to file an annual report on Form 10-K, 20-F or 40-F, and that engage in the commercial development of oil, natural gas or minerals. Issuers that qualify as smaller reporting companies and emerging growth companies are exempt from the rules to the extent that they are not subject to an alternative reporting regime (see below) that has been deemed by the SEC to require disclosure that satisfies the required transparency objectives.

The term “commercial development of oil, natural gas, or minerals” is defined as exploration, extraction, processing, and export of oil, natural gas, or minerals, or the acquisition of a license for any such activity. The definition is specifically designed to capture only those activities that are directly related to the commercial development of oil, natural gas and minerals and excludes any activities ancillary or preparatory to such commercial development. To assist issuers in determining the scope of activities covered by the definition, the final rules provide detailed guidance on the individual terms within the definition.

In addition to reporting its own payments, a resource extraction issuer is also required to disclose payments made by a subsidiary or entity controlled by the issuer. For purposes of the rules, control is determined by reference to financial consolidation principles that the issuer applies to the audited financial statements in its annual reports. The SEC specifically declined to include a “significant influence” test for determining control in addition to the accounting consolidation principles.

Under the final rules, resource extraction issuers will not be required to disclose the proportionate amount of the payments made by proportionately consolidated entities or operations.

In addition, the final rules clarify that for joint ventures where no single party has control, a resource extraction issuer that is the operator of the venture or arrangement and makes payments to governments for the entire venture or arrangement, on behalf of its non-operator members, must report all of the payments. Non-operator members of the joint venture will not be required to report payments that they make to reimburse the operator for their share of the payments, but will be required to report payments that they, as resource extraction issuers, make directly.

Payments Subject to Disclosure

Under the final rules, resource extraction issuers are required to disclose payments that are:

- made to the U.S. federal government or a foreign government;
- made to further the commercial development of oil, natural gas or minerals;
- not de minimis; and
- any of the types of payments specified in the rules (taxes, royalties, fees, production entitlements, bonuses, dividends, payment for infrastructure improvements and community and social responsibility payments (CSRs) that are required by law or contract).

The final rules include in the definition of “foreign government” any foreign national or subnational government, department, agency or instrumentality thereof and any company at least majority-owned by a foreign government. Subnational governments include those of a state, province, department, county, district, municipality or territory.

Under the final rules, a “not de minimis” payment means any payment, whether made as a single payment or a series of related payments, that equals or exceeds \$100,000, or its equivalent in the resource extraction issuer’s reporting currency. For any arrangement providing for periodic payments or installments, an issuer must 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 accordingly, whether disclosure is required. The final Form SD provides that the payment disclosure must be presented on a cash basis instead of an accrual basis and need not be audited.

Projects

The final rules require a resource extraction issuer to disclose payments made to foreign governments relating to the commercial development of oil, natural gas or minerals by type and total amount per project. One of the key changes from the 2016 disapproved version of the rule is the definition of “project,” which was one of the two key aspects of the rule (the other being publication of payments versus anonymized compilations) that the SEC felt it would need to change in order to satisfy the requirements of the CRA that the new rule not be “substantially the same” as the prior disapproved version. The SEC opted to move away from the more granular contract-level project definition, though it noted that in doing so, it is deviating from the contract-based definition adopted under the regimes referred to below under “Alternative Reporting.”

The term “project” is defined using the following three criteria:

- the *type of resource* being commercially developed (*i.e.*, oil, natural gas, gold, etc.; issuers will not be required to describe the specific type or quality of oil or natural gas or distinguish between subcategories of the same mineral type);
- the *method of extraction* (*i.e.*, whether extracted through the use of a well, an open pit or underground mine; specificity beyond that is will not be required, *e.g.*, issuers need not specify what type of well); and
- the *major subnational political jurisdiction* where the commercial development of the resource is taking place.

The third prong will require an issuer to disclose only to the level of major subnational jurisdiction (*e.g.*, state, province, district, region, territory) in which the resource extraction activities are occurring. An issuer must provide an electronic tag for both the country and the major subnational political jurisdiction in which the extractive activities are occurring that is consistent with the International Organization for Standardization code pertaining to countries and their major subdivisions. For offshore projects, the identification of the major subnational political jurisdiction where the commercial development of the resource is taking place should include the body of water in which the project is located, using the smallest

body of water applicable (e.g., gulf, bay, sea), as well as the nearest major subnational jurisdiction. In addition, if the project is equidistant from two major subnational jurisdictions, the issuer may disclose both such jurisdictions.

Commercial development activities involving multiple resource types or extraction methods can be treated as a single project if such activities are located in the same major subnational political jurisdiction. The issuer will be required to describe each type of resource that is being commercially developed and each method of extraction used for that project. The geography of a commercial development could cross borders and generate payment obligations in multiple major subnational political jurisdictions. In such a case, the final rules will require the issuer to treat the activities in each major subnational political jurisdiction as separate projects.

Aggregation of Payments

Under the final rules, an issuer will still be able to aggregate payments by payment type when disclosing payments made at a level below the major subnational government level. It will, however, now be required to disclose the aggregated amount paid to each subnational political jurisdiction, and identify such subnational political jurisdiction. As a result, an issuer's reporting obligations at below major subnational government levels will be the same as its reporting obligations at the major subnational government level. The SEC cites the example of extractive operations in the three oil sands regions of Alberta, Canada (the Regional Municipality of Wood Buffalo, Northern Sunrise County and the Municipality of Cold Lake), for which an issuer would be required to identify each such subnational government entity, as well as aggregate and report all of its fees paid for environmental and other permits to each such entity. For example, an issuer could aggregate all of the royalties arising from its operations in the three oil sands areas paid at the provincial level but will be required to disclose the particular agency payee, e.g., the Alberta Department of Energy. Additionally, such issuer would need to separately identify payments to any municipal or regional authority for environmental and other permits and fees.

Exemptions

Extraction payments disclosure is not required in situations where it would be prohibited by:

- foreign law – where the disclosure is not possible without violating the laws of the jurisdiction where the project is located; or
- preexisting contractual terms – applies only to contracts in which such terms are expressly included in writing prior to the entry into force of the final rules.

Issuers are not required to apply to the SEC for exemption relief in connection with these exemptions, but they need to take reasonable steps to seek and use any other available exemption or relief, failing which

they will need to provide specific disclosures about their eligibility for the exemption, including identifying the jurisdiction and furnishing as an exhibit to Form SD a legal opinion from counsel opining on the inability of the issuer to provide the required disclosure without violating the foreign jurisdiction's laws or the applicable contractual terms.

The SEC has discretion to grant additional exemptions on a case-by-case basis, upon receipt of a written request from an issuer describing the particular payments disclosures that the issuer seeks to omit and the specific facts and circumstances that would warrant the exemption.

Delayed Reporting and Transitional Relief

Issuers will not be required to report payments related to exploratory activities in the Form SD for the fiscal year in which payments are made. Instead, an issuer may delay reporting such payments until it submits a Form SD for the fiscal year following the fiscal year in which the payments were made. For purposes of this provision, the SEC will consider payments to be related to exploratory activities if they are made as part of the process of: identifying areas that may warrant examination; examining specific areas that are considered to have prospects of containing oil and gas reserves; or conducting a mineral exploration program. In all cases, exploratory activities will be limited to activities conducted prior to the commercial development of the oil, natural gas or minerals that are the subject of the exploratory activities.

The SEC has also provided transitional relief, in the form of one-year delayed reporting, for recently acquired companies that were not previously subject to Section 13(q) or an alternative reporting regime deemed by the SEC to satisfy the transparency objectives of Section 13(q), as well as for issuers that completed their initial public offering in the United States in their last full fiscal year.

Method of Disclosure

The final rules require that resource extraction issuers publicly submit the payment information disclosure, including the issuer's name, on Form SD that will be furnished to (rather than filed with) the SEC, through the searchable, online EDGAR system. The required disclosure elements need to be provided in XBRL format using specified electronic tags, which will make it easier for users to extract, aggregate and analyze the information. The SEC specifically opted to include the resource payments disclosure in Form SD rather than in a Form 10-K, 20-F or 40-F in order to exclude this disclosure from the coverage by the officer certifications required by Exchange Act Rules 13a-14 and 15d-14.

Alternative Reporting

In light of the fact that other jurisdictions may also have in place disclosure laws relating to resource extraction payments, issuers will be able to meet the requirements of the final rules by providing disclosure

that complies with a foreign jurisdiction's resource extraction payment disclosure requirements if such requirements are deemed equivalent by the SEC.

The SEC order accompanying the final rules designates the following five resource extraction payment disclosure regimes as alternative reporting regimes that satisfy the required transparency objectives: (i) Canada's Extractive Sector Transparency Measures; (ii) the EU Accounting Directive 2013/34/EU; (iii) the EU Transparency Directive 2013/50/EU; (iv) the UK Reports on Payment to Governments Regulation 2014; and (v) the Norwegian Regulation on Country-by-Country Reporting. Accordingly, a resource extraction issuer that submits a report complying with the reporting requirement of any of these specified regimes will be deemed to satisfy the requirements under the SEC resource extraction payment disclosure rules.

Issuers using alternative reports will need to provide English translation of such reports and the reports will need to be tagged using XBRL.

Timing

A resource extraction issuer will be required to comply with the new annual reporting requirement starting with its fiscal year ending no earlier than two years after the effective date of the final rules. Following the two-year transition period, Form SD will be due no later than 270 days after the end of an issuer's most recently completed fiscal year.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Mark S. Bergman
+44-20-7367-1601
mbergman@paulweiss.com

Christopher J. Cummings
+1-212-373-3434
ccummings@paulweiss.com

Andrew J. Foley
+1-212-373-3078
afoley@paulweiss.com

Adam M. Givertz
+1-212-373-3224
agivertz@paulweiss.com

Raphael M. Russo
+1-212-373-3309
rrusso@paulweiss.com

Tracey A. Zacccone
+1-212-373-3085
tzacccone@paulweiss.com

Securities Practice Management Attorney Monika G. Kisłowska and Practice Management Consultant Jane Danek contributed to this Client Memorandum.