
The Reports on Payments to Governments Regulations 2014

post-implementation review

Department for Business, Energy and Industrial Strategy

RPC rating: fit for purpose

Description of proposal

The post-implementation review (PIR) is on The Reports on Payments to Governments Regulations 2014, as amended in 2015. The regulations require UK-registered companies engaged in the extraction of oil, minerals and natural gas and in the logging of primary forests to disclose, on an annual basis, the details of payments made to governments regarding this activity. The regulations were intended to bring greater transparency and accountability to revenue flows to governments of resource-rich countries.

The regulations implement chapter 10 of the EU accounting directive (2013/34). They came into force in the UK on 1 December 2014. This was a year earlier than required by the directive but it was in line with the UK Government's commitment to quick implementation made at a G8 summit in 2014. The regulations apply to financial years beginning on or after 1 January 2015.

Impacts of proposal

To inform the PIR, the Department commissioned PricewaterhouseCoopers (PwC) to undertake a full review of the impacts of the new reporting regime. The research assessed the costs and benefits to companies in scope of the legislation and impacts on their investors and any civil society organisations (CSOs) that have a particular interest in this legislation. Responses were collected via telephone interviews, an interactive electronic form and some face to face interviews between August and October 2017. Of the 91 companies that have submitted reports, 32 participated in the PwC research; they represent a broad distribution of organisations by both revenue and employee size. The PIR states that written submissions from stakeholder groups and other interested parties were also considered in the development of the review.

Companies in scope

The Department's impact assessment (IA) estimated that 251 companies would be in scope. This is well in excess of the 91 companies that have so far submitted reports to Companies House and/or the Financial Conduct Authority. The Department explains that this could be "*...in part attributed to the fact that the IA accounted for the complexity of ownership structures (group structures) in determining the number of reporting entities; and the possibility that not all companies in scope will necessarily have made payments to Governments during the period considered in the research*" (paragraph 23, page 6).

Costs to companies in scope

The Department explains that 84 per cent of the companies indicated that they did not actively capture compliance costs, although 15 companies provided actual or estimated costs for one-off impacts and 15 (not the same 15 companies) provided recurring cost figures. Assuming that the size distribution of these companies is representative of the size distribution for all companies in scope, the Department estimates aggregate costs of compliance at £52.5 million. This is significantly higher than the IA's estimate of £19.7 million. The Department states that this difference is "*...most likely due to the fact that in the IA, costs were aggregated based on the separate filing activities of subsidiaries and their parent companies, based on data extrapolated from four companies. This small sample may not have covered the largest companies in the distribution and may have also underestimated costs to subsidiaries, thereby underestimating the overall impact.*" (paragraph 33, page 10).

The PIR provides a breakdown of this cost, with the largest categories being 'understanding the regulatory requirements' (32 per cent), 'data extraction by local teams' (17 per cent) and 'preparation of the consolidated report' (16 per cent). The Department indicates that this supports the expectation in the IA that familiarisation would be a significant cost. The PIR also provides a breakdown of costs by company size and by factors driving compliance costs (such as number of payment types, projects, countries etc). The PIR additionally provides limited information on external costs incurred by companies (such as legal fees). These do not appear to be included in the above aggregate estimates and the Department notes that they were not accounted for in the IA.

Wider impacts

Under 'wider impacts', the PIR considers the impacts associated with two features of the regulations where it appears that the UK had more discretion in implementation. First, on early implementation, the PIR reports that 72 per cent of companies indicated that this did not impose additional costs, but some companies indicated that it put UK companies at a competitive disadvantage compared to their peer companies that were not subject to similar reporting requirements. Second, the PIR investigated the impact of the UK's decision not to exempt from reporting operations of UK-based companies in countries that prohibit disclosure in criminal law. The PIR reports that "*Close to 50 per cent [of respondents] indicated that they had no issues in any of the countries in which they made payments*", although "*Some companies have indicated that in some cases, there was a need to assess any conflict of law around disclosure in different jurisdictions, and to manage relationships in host countries*" (paragraphs 42-43, page 12).

Benefits

The Department reports that "*The IA outlined expected benefits to UK companies within the context of improved governance, widened economic opportunities, increased political stability, and reduced corruption.*" (paragraph 45, page 12). The IA also considered that the proposal would allow investors easier access to information with which they could "*...more effectively model cash-flows, assess political risks and acquisition costs, increase their managerial effectiveness, and ultimately, materially and substantially improve their investment decision-making.*" (paragraph 46, page 12).

However, the PIR notes that "*Due to the relatively short time period between the implementation of the Regulations and the research conducted for this review, many companies and their investors are yet to realise any of these positive impacts.*" (paragraph 47, page 12). Nevertheless, the PIR provides fairly detailed information on current, and expected, financial and non-financial benefits to companies, citizens of host countries and on the views of CSOs (pages 12-19). 19 per cent of businesses saw a positive current influence of the regulations on 'the business environment', rising to 25 per cent over the next 3-5 years. However, over 80 per cent saw neither a positive nor negative impact of the regulations on 'business opportunities' or 'volume of extraction'. More than 50 per cent indicated that they experienced no improvement in their reputation amongst investors, trading partners, and the wider society as a result of the regulation. CSOs were, as expected, more positive about the impact of the regulations and provided country-specific examples

where mandatory reporting had been valuable, for example where reforming elements of government have invited civil society organisations to work with them in analysing the data from mandatory reporting in order to fight corruption (appendices A and B).

Quality of submission

The regulations have been in place for only a relatively short period but the PIR includes sufficient evidence to support the retention of the regulations at this time. The commissioning of the PwC research has resulted in useful and fairly-detailed information on costs incurred by businesses so far. The Department compares these costs against the much lower IA estimates. The research results are presented clearly, with many helpful charts. The focus of the PIR on the impact of the early implementation and on the absence of an exemption clause is helpful, since these appear to be areas of UK policy discretion. The Department also helpfully highlights some difficulties that companies are having with the submission process and notes that the Department is drawing this to the attention of Companies House. The Department states that the findings of the review will contribute to a review of Chapter 10 of the Accounting Directive by the European Commission, expected in 2019.

There are a number of areas where the PIR could be improved. These are outlined below:

Conclusions and next steps. Given the early stage of the policy and limited evidence so far on benefits, the PIR could be more measured in its positive assessment of the impacts of the policy. In particular, the Department should provide support for its statement that “*There is every indication that in the medium to long term, the benefits of the regulations would outweigh the costs imposed by it.*” (paragraph 83, page 22), particularly given the much higher than expected costs and that it appears too early to judge the likely scale of benefits. The statement in paragraph 84 (page 12) that “*The conclusions in this review are based on early findings, and further company reporting and experience of the requirements is necessary before any final conclusions of the effectiveness of this reporting regime can be drawn.*” appears to be more measured. The PIR would benefit from setting out the next steps in the evaluation of the measure and when more substantial conclusions will be drawn. The present PIR provides a basis for retaining the regulations only until these final conclusions can be drawn.

Impact on investors. The PIR would benefit from addressing whether investors have shown signs of responding to the reports, how far benefits to investors have been realised and how awareness amongst investors might be raised (paragraph 47, page 12).

Representativeness of the companies that provided cost information. The PIR could address not just whether the companies that provided compliance costs are representative of the size distribution for all companies in scope but also whether their compliance costs are representative, which may depend on factors other than size.

Impact of reporting requirements in other EU countries and other major economies. The PIR could be clearer in whether it has taken full account of possible evidence and confounding effect of parallel measures in other countries, such as France and Canada, and of multinational initiatives (e.g. The Extractive Industries Transparency Initiative).

Evidence to support the views of CSOs. Although the country-specific examples are useful, the PIR could seek, and present, more evidence to support the statements (for example on page 17) from CSOs on the effectiveness of the regulations.

UK government use of the information disclosed. In particular, whether there have been any regulatory actions, or evidence that this has influenced lawsuits and court judgments.

Comparison to IA and lessons learned. The PIR includes a useful comparison against the IA. This would benefit from further clarification in places and from drawing lessons for future IAs, for example in terms of extrapolating aggregate cost estimates from a very small number of companies (paragraph 33, page 11).

Departmental recommendation	Retain
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RPC assessment

Is the evidence in the PIR sufficiently robust to support the departmental recommendation?	Yes
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Anthony Browne, Chairman