

PARLIAMENTARY DEBATES

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OFFICIAL REPORT

Seventh Delegated Legislation Committee

DRAFT REPORTS ON PAYMENTS TO
GOVERNMENTS REGULATIONS 2014

Tuesday 25 November 2014

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The Committee consisted of the following Members:

Chair: MRS ANNE MAIN

- | | |
|---|---|
| Austin, Ian (<i>Dudley North</i>) (Lab) | † Munt, Tessa (<i>Wells</i>) (LD) |
| † Doughty, Stephen (<i>Cardiff South and Penarth</i>) (Lab/
Co-op) | † Nuttall, Mr David (<i>Bury North</i>) (Con) |
| † Harris, Rebecca (<i>Castle Point</i>) (Con) | Simpson, David (<i>Upper Bann</i>) (DUP) |
| † Heaton-Harris, Chris (<i>Daventry</i>) (Con) | † Skinner, Mr Dennis (<i>Bolsover</i>) (Lab) |
| † Hillier, Meg (<i>Hackney South and Shoreditch</i>) (Lab/
Co-op) | † Stride, Mel (<i>Central Devon</i>) (Con) |
| † James, Margot (<i>Stourbridge</i>) (Con) | † Swinson, Jo (<i>Parliamentary Under-Secretary of State
for Business, Innovation and Skills</i>) |
| † Jones, Mr David (<i>Clwyd West</i>) (Con) | Vaz, Valerie (<i>Walsall South</i>) (Lab) |
| † Lumley, Karen (<i>Redditch</i>) (Con) | † Wright, Mr Iain (<i>Hartlepool</i>) (Lab) |
| † McCartney, Jason (<i>Colne Valley</i>) (Con) | Marek Kubala, <i>Committee Clerk</i> |
| Meacher, Mr Michael (<i>Oldham West and Royton</i>)
(Lab) | † attended the Committee |

Seventh Delegated Legislation Committee

Tuesday 25 November 2014

[MRS ANNE MAIN *in the Chair*]

Draft Reports on Payments to Governments Regulations 2014

2.30 pm

The Parliamentary Under-Secretary of State for Business, Innovation and Skills (Jo Swinson): I beg to move,

That the Committee has considered the draft Reports on Payments to Governments Regulations 2014.

It is a great pleasure to serve under your chairmanship, Mrs Main, perhaps for the first time. It is delightful to do so.

The draft regulations play an important role in achieving the Government's goal of raising global standards on transparency reporting. Many of the world's poorest countries have huge reserves of valuable natural resources, but their citizens often remain extremely poor. The significant payments made by extractive companies to Governments have the potential to boost economic growth and to help resource-rich developing countries to pull themselves out of poverty.

The UK is demonstrating strong international leadership to improve governance of the extractive industries. Norway has similar legislation in place; Canada is on track to implement new law this year; and the USA expects to have rules in place next year. We are delivering on the commitment that we made during the UK's G8 presidency in 2013 to implement quickly extractive reporting requirements. That is alongside our commitment to implement the extractive industries transparency initiative—we recently celebrated candidacy status being awarded to the UK.

Transparency makes good business sense. Investors must consider the operations of a company in the round. Some companies already make information available and they say that it is valued by their investors.

The draft regulations are a result of the agreement of the European Union's accounting directive. We recognise not only the importance of a strong and effective reporting requirement but the fact that the burdens imposed on industry should be proportionate. During negotiations, the UK worked closely with industry and civil society representatives in a particularly fruitful working relationship that continues as part of the stakeholder group on the EITI. That was especially important when agreeing the definition of project-level reporting.

The UK also played a key role in ensuring that the directive has an equivalence provision, which will ensure that companies do not need to provide different reports to multiple authorities in different jurisdictions that none the less have similar rules. That will be particularly important for companies listed in both the US and the EU.

Having explained the background to the draft regulations, I turn to the content. Many of the requirements are fixed by the directive. That approach is necessary to

ensure that we have certainty and consistency throughout the EU. Companies must report on payments made to all Governments at all levels, whether national, regional or local, along with Government agencies and state-owned companies. The report must detail information of the payments made project by project. The definition of "project" reflects how industry manages and reports on its business activities.

The payments to be reported are listed in the draft regulations. Companies are required to report any payments made under those headings. Member states are not offered any flexibility to grant exemptions from reporting if a company and its payments fall within the scope of the measure. Companies are only required to report payments over the threshold of £86,000. The regulations also make it clear that one payment may not be split to avoid reporting. For example, if a payment of £100,000 were artificially split into two payments of £50,000, the full amount of £100,000 would need to be reported.

In many countries, payments to Governments are commonly paid in kind. An in-kind payment may include improvements to infrastructure, such as the building of a new road, and such payments must be included in the report, with the value attributed to any in-kind payment. To avoid doubt, the basis for how that given value has been arrived at must be set out.

The directive requires large companies and public interest companies active in the extractives sector to prepare a report. The transparency directive applies the same requirements to all companies listed on EU-regulated markets. The Financial Conduct Authority has recently consulted on new rules that refer to the draft regulations, and listed companies will be required to report on the same basis, although to a different timetable.

Consultation on the draft regulations took place between March and May of this year. It considered the areas in which the directive offered flexibility, including the date of the first reporting period; the period allowed for the preparation and publication of the report; and the reporting format. In line with UK commitments, companies will be required to prepare reports for financial years that begin from 1 January 2015. That will mean that the first reports will be published in 2016.

To ensure sufficient time to gather the information, companies are permitted 11 months after the end of the company financial year to complete the reports. Listed companies will have up to six months to report, which gives an additional two months compared with the time available for their annual report. It is vital that the reporting format is as simple as possible, to keep administrative burdens to a minimum. Companies House is working alongside industry to agree the format. Requiring electronic reporting will facilitate efficient receipt and sharing of data in the reports.

The Companies Act 2006 requires companies to publish information. Compliance and accuracy are achieved by using effective enforcement tools, supplemented by public scrutiny. We will apply the same approach to the enforcement of the regulations. We want to ensure that all companies are able to report in a simple and effective way. Should a company be challenged for failure to publish or prepare a report, or for delivering a factually incorrect report, the registrar will first ask it to explain the reasons for, for example, not delivering the report. Those could include the fact that no payments to Governments were made in a given year, or that a

company is reporting as part of a parent company's consolidated report. In line with other financial reporting requirements, companies will be required to report on a consolidated basis if they are part of a group.

If it is established that a report should be prepared, the company will be given the opportunity to comply. If it fails to do so, the law sets out a penalty regime. That regime has been considered carefully and is consistent with that for similar reporting requirements in the Companies Act 2006. Failure to prepare and publish a report could result in either a fine or a prison sentence.

To help companies with the practical aspects of preparing reports, international representative organisations of the oil and mining industries have drafted a combined guidance document, which is currently being consulted on and is available on the website of the Department for Business, Innovation and Skills. BIS is also working with the Foreign and Commonwealth Office to raise awareness of the EU directive and the UK regulations in countries around the world. By explaining the rationale for reporting payments we think we will get the most effective outcome.

I hope that hon. Members support the draft regulations. I also hope they see that the UK is setting an example in extractives transparency. The industry is supportive of that agenda, and its response to the consultation clearly showed that transparency was an important tool in improving governance. The regulations will improve global standards in transparency reporting in the extractive industries, which I hope will lead to many millions of people moving out of poverty. I commend the regulations to the Committee.

2.37 pm

Mr Iain Wright (Hartlepool) (Lab): As the Minister said, it is a pleasure to serve under your chairmanship, Mrs Main.

I will not detain the Committee for long. I commend the regulations, which are good for business and for transparency, and are about doing the right thing. I pay tribute to the Minister—I can see her fingerprints all over the regulations, and that is a good and positive thing. Her work to put this matter on the Government's agenda is welcome.

I have a number of questions to put to the Minister. Regulation 2 is about interpretation, and mentions what could be exempted from the payments. I draw the Minister's attention to paragraph (1) and what it says about payments. The provision says that dividends can be accepted under the normal terms of trade,

"other than dividends paid by an undertaking to a government as an ordinary shareholder of that undertaking, where...the dividend is paid to the government on the same terms as to other ordinary shareholders, and...the dividend is not paid in lieu of production entitlements or royalties".

That all seems well and good, but I am concerned about the risk of dividends being used as a means of getting round the regulations. Will she set out what has been going on in that regard and comment on whether dividends will be explored as part of the general anti-avoidance rule?

Once an accountant, always an accountant, Mrs Main, and I want to talk about the accruals process. *[Interruption.]* I am glad I am keeping everybody—*[Interruption.]* My objective is to bore everybody into submission and then

call a Division. I am very good at that. The accruals process—I am back on firm ground—is the posting of the actual amount in relation to when in the year that amount is accrued relative to the actual activity. I am interested in that with regard to the regulations because I want to make sure that things are as transparent, open and understandable as possible, and so would like to hear what the Minister thinks will happen in that regard.

First, as I understand the regulations, a payment need not be taken into account in the report if it is a single payment of an amount of less than £86,000 or if it forms part of a series of related payments within a financial year, the total amount of which is less than £86,000. What would happen with, say, a £750,000 payment over 10 years? Would that not need to be apportioned to £75,000 a year? What would the report actually state—£75,000 or that up-front payment of £750,000?

Secondly, the Minister said that quite a substantial consultation exercise took place earlier this year. The Government's intent was made clear with their response in August this year. The regulations, if passed by the House and the other place, will come into effect on 1 December. Does she have any evidence that people are trying to game the system by making quite substantial payments now, before the regulations come into effect? Has she taken any active steps to assess avoidance of the regulations?

Once an accountant, always an accountant: I will now talk about the audit process. Will the report be subject to audit through the regular process? My understanding is that that is not the case, because it was seen to result in an excessive cost for business. How can an investor take reassurance from the report if it has not been independently verified, perhaps by the auditor of the organisation?

Turning to other reporting jurisdictions, reporting requirements are improving and advancing in places such as the US, Canada and Norway. The best way to manage the cost to industry is to encourage consistent global reporting standards that will help to level the playing field with UK companies and avoid a disproportionate impact on UK-based businesses. It also helps with the cost of compliance. What efforts are the Government making to encourage the US Securities and Exchange Commission and other regulators to pass reporting rules that are equivalent to those coming into force in the UK? In relation to the transatlantic trade and investment partnership, is this being actively discussed as part of that north American-European trade treaty?

Stephen Doughty (Cardiff South and Penarth) (Lab/Co-op): My hon. Friend makes an important point. Would he be interested to know, as I would be, what steps the Government propose at an international level with regards to countries such as China? Some companies operating from China are heavily involved in the extractives industry, particularly in Africa, and are not subject to the same sort of reporting requirements that I am glad to see being introduced here by the Government and the European Union.

Mr Wright: I pay tribute to my hon. Friend for all his hard work on this. He makes an important point about China and the fact that there is almost a 21st-century

[Mr Iain Wright]

scramble for Africa among Chinese companies. It would be interesting to know what the Minister is doing on that in the international community.

Regulation 11 talks about exemption from the consolidated report. In her opening remarks, the Minister discussed subsidiary companies that will be exempt from the regulations. Will she give us an outline of how many companies will be affected? On enforcement, will she give us her assurance that the regulations will be enacted and, crucially, enforced in a way that promotes these outcomes? Will the reporting template and industry guidance being prepared to accompany the regulations reflect the robust standard of payment reporting mandated by the accounting directive and provided for by her leadership? Will any deliberately misleading reporting of payments be investigated and severely penalised by BIS to avoid a lack of compliance with the regulations?

Finally, I want to talk briefly about the Commission's work on breaking the links between the trade and extraction of minerals and the financing of armed conflicts. I know that the Minister takes a keen interest in that. We should be building on the payment transparency in the extractives industries and elsewhere that is included in the regulations by calling for mandatory due diligence and reporting. Will she confirm how the Government are promoting transparency about the issue of conflict minerals, in the context of the weak draft regulations proposed by the European Commission? Is the Minister promoting a stronger regulation that includes mandatory reporting requirements for companies sourcing materials from conflict-affected and high-risk areas in accordance with the OECD due diligence guidance?

Having asked those questions, I welcome these regulations and I praise what the Minister has done personally to make sure that the UK is at the cutting edge of promoting transparency in this field. I am interested to hear her response.

2.44 pm

Jo Swinson: I am delighted that the hon. Member for Hartlepool is, in general, supportive of these measures, as I hope the rest of the Committee is. I am very happy to respond to his points; it is always a true delight to respond to an accountant on the Committee. I thank him for his kind words about my involvement. I am very proud to be involved in these regulations. It is also fair to recognise that there has been significant leadership from the Prime Minister at the G8 summit last year and, throughout Government, there has been great commitment on these issues. The Opposition's support has also been very welcome.

Stephen Doughty: I, too, pay tribute to the Minister's work. Will she also tribute to the many international organisations, such as Publish What You Pay, Transparency International, Global Witness, CAFOD, Christian Aid, Action Aid and many others, which have exposed many of the cases which led to the need to bring about these regulations? If it was not for their work, we would not know of many of the shocking abuses that have gone on in these industries.

Jo Swinson: The hon. Gentleman is absolutely right to highlight the excellent work of many campaigning organisations, which helped ensure strong rules coming

out of the United States which, I think, strengthened the hand of those participating in the EU discussions. That is a really good example of campaigning. I referred briefly to work on a separate but related initiative, the extractive industries transparency initiative, where we are working with many campaigners and industry. The positive and constructive way in which those groups and individuals have worked together is commendable and that is why we have made such progress.

On the issue of dividends being used as avoidance, we will carry out a review three years after the regulations come into force. That will ensure that all payments are correct and that there are no loopholes being used in the way that the hon. Member for Hartlepool suggested. The wording in our regulations is copied directly from the directive, and that consistency is sensible, but if we find in the review period that it is being used for avoidance that will be looked at.

On the accruals process mentioned by the hon. Member for Hartlepool, payments need to be reported when they are on the balance sheet for that financial year. He raised the scenario of whether a large payment over a period of 10 years would be captured if in any individual year it was below the amount. If the payment split out over that period of time is under the £86,000 threshold in a particular year, that does not have to be reported. If something had been done deliberately to create avoidance and that is not an accurate reflection of what has taken place, then of course that would not apply.

On gaming, the hon. Gentleman will be glad to hear that there is no evidence that what he suggested has taken place. Industry is well versed on the direction Government are taking on this, and on our progress, it is generally supportive of the measures that we have introduced, and it recognises the serious concerns expressed by the public. He also raised the issue of audits—I expected nothing less from him, given his former work in audit. The total payments that are made will be part of the audited accounts of the particular company. It would not be accurate to say that there is no audit process that looks at this, but the reports provide much more detailed information, and the best way for companies to be held to account is through the extensive public scrutiny that will no doubt take place. That is part of the point of this transparency initiative and why we believe it is good for business.

On consistency of global reporting, a point which was also raised by the hon. Member for Cardiff South and Penarth, we want to get to a stage where all companies and countries participate in the transparency measures. We have to show UK leadership. It is great that the US and the EU are also taking great steps, but we should not suggest that progress is only happening in those places. The extractive industries transparency initiative has 48 countries participating in the process. It includes some of the more developed countries, but also many countries in Africa and other parts of the world, which is a good sign that the initiative is being taken increasingly seriously by other countries. The UK's EITI candidacy puts us in a stronger position internationally to encourage other countries to sign up and take the issues seriously.

Stephen Doughty: Does the Minister agree that, as well as the reporting and transparency of information, it is crucial that Governments, including the UK and

the European Commission, support Governments in developing countries so that they can scrutinise companies that operate in their countries by strengthening Parliaments, Treasuries and Ministries for natural resources? Will she ask one of her colleagues at the Department for International Development to write to us about what action the UK is taking in that regard?

Jo Swinson: The hon. Gentleman is quite right. The skills needed within countries are important. He is right to mention Ministries and civil servants, but civil society is also important. The Government already undertake a significant amount of work on this issue through DFID, and I am sure my colleagues will be happy to update him on the specifics. I also know from my previous role on the board of the Westminster Foundation for Democracy that that organisation undertakes significant work to strengthen civil society and democratic organisations within countries so that they can improve their campaigning skills and their ability to hold Governments to account. That part of the process is absolutely vital.

On the TTIP negotiations not being in the specific negotiations, I will write to the hon. Member for Hartlepool in response to his question about how that has played into the discussions, if indeed it has been specifically mentioned. On the exemption, where a parent company will make a declaration, our current estimate is that 38

companies would fall into that category. Obviously, that number can change over time as company structures change.

On the issue of whether people who are deliberately misleading in their reporting will be strongly penalised, the answer is yes. We have significant criminal sanctions. As I mentioned, that is not the first stop. We recognise that there might be circumstances in which a company, for whatever reason, believes that there is no need to report. In the first instance, the company will be asked why compliance has not happened and whether there is a reason, and it will have an opportunity to make it happen. Public scrutiny and transparency will be a key driver. Clearly, if companies deliberately try to defy the regulations and deliberately try to mislead, that would be against the entire spirit and letter of the law, and significant sanctions are available.

I will endeavour to write to the hon. Member for Hartlepool about the EU proposal on conflict minerals. I am not familiar with the details, and I am keen to get the answer right, so I will write to him. I hope my comments have satisfied the Committee and that hon. Members will support the regulations.

Question put and agreed to.

2.53 pm

Committee rose.

