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Transparency Matters

Disclosure of payments to governments
by Chinese extractive companies



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1. Executive Summary

China's supply of natural resources is a key element in the drive to sustain economic growth and long-term energy security. However, many resource-rich countries that China does business with have fallen victim to the 'resource curse' – the paradox that countries and regions with an abundance of minerals and hydrocarbons tend to have less economic growth, more conflict and corruption, and worse development outcomes than countries with fewer natural resources. As a result, Chinese extractive companies face particular investment and security risks as they extract from resource curse affected countries and regions, making them vulnerable to corruption and instability.

Recent cases of these risks affecting Chinese interests include:

- Unanswered questions in the Democratic Republic of Congo regarding the accounting of nearly US\$24 million of the Chinese government's "signature bonus" payment for a major resource-for-infrastructure agreement. A Congolese parliamentary commission alleged that it was diverted into an offshore company by Congolese partners.¹
- International Monetary Fund estimates that, between 2007 and 2010, US\$32 billion in public funds went missing in oil-rich Angola, a country with significant Chinese extractive company activities.²
- A lack of transparency in oil operations in Sudan and South Sudan operated by Chinese and other companies has fuelled mistrust and conflict between the two countries, leading in early 2012 to the total shutdown of production in South Sudan and the military occupation of a major processing facility along the border in Sudan. Both actions have come with a significant cost to Chinese companies and the international oil market.³

Ensuring good resource management and preventing corruption is critical for Chinese companies in running respected, responsible and sustainable operations. Mr Xi Jinping, the newly-appointed Chairman of the Chinese Communist Party, has spoken strongly about the risk that corruption plays to China's national wellbeing and security.

Greater transparency in the extractive industries is an important first step towards tackling corruption. An

emerging global consensus holds that transparency is needed in the payments made by extractive companies to governments in order to help prevent corruption and the conflict associated with it. Disclosure of revenues paid by extractive companies to governments has multiple benefits for industry, investors, stock exchanges and host populations in reducing corruption and creating a more predictable investment environment.

Governments, citizens, investors and progressive companies around the world are pushing for more effective transparency in natural resource deals. Stock exchange regulations requiring payment disclosure for listed companies have been developed in the US, EU and Hong Kong over the past two years (see chapter two for details and benefits of these). These measures compliment the voluntary Extractive Industries Transparency Initiative to which 30 countries have signed-up. The EITI obliges governments to publish payments that they receive from extractive companies and companies to publish the payments that they make to governments under monitoring by civil society and independent auditing.

The Shanghai Stock Exchange plays an important role in setting the standard for extractive industry activities and leads all other Asian exchanges in terms of extractive industry market value. Its success is strongly influenced by the activities of its extractive sector.

This report contains two original pieces of research exploring the potential role of the Shanghai Stock Exchange (SSE) to improve extractive company disclosure and transparency measures.

Firstly, the report analyses all the available government payment information of the 15 largest extractive companies with international operations listed on the SSE (see Chapter Four). The study finds that, although a few companies such as PetroChina, China Oilfield Services Limited and Zijin Mining stand out in the depth of their reporting, financial information provided by most companies is limited and in a format which makes it difficult to compare companies.

Among the 15 companies covered in this study, five companies reported (limited) information about overseas tax payments and ten companies disclosed some information linked to overseas revenues, such as

aggregated or country specific revenue gained overseas, total amount or percentage of income tax paid to host government.

The reporting of common domestic tax items demonstrates that companies clearly have the information to hand to improve their reporting. However, there is little standardisation of reporting and important payment types are omitted. The lack of clear financial and payment information prevents investors from obtaining anything more than a rudimentary understanding of the operations of the companies analysed.

Voluntary disclosure on social contribution value per share (SCVPS) is an initiative that the SSE launched in 2008, and one of the few reporting items that provides stakeholders with an insight of companies' impact on society. Although SCVPS calculations remain broadly consistent for individual companies for the two years under review, they do not seem in any way comparable between companies, even within the same industry. This makes its utility debatable and is an issue that could be significantly improved with better guidance.

The report also analyses the survey responses of 24 different stakeholders of the Chinese extractive industry, including asset managers, extractive industry representatives, academics, and international and domestic organizations to the idea of the SSE implementing improved country-by-country reporting requirements (see Chapter Five). A significant proportion of Chinese and international respondents believe that increased disclosure of payment information would improve the global reputation of Chinese extractive companies and help investors better analyse company risks. Nearly half of international respondents explicitly supported the SSE synchronizing its regulations with the HKEx, the US and pending requirements in the EU.

The most common concern voiced against such proposals was that expanded government payment reporting would reduce the competitiveness of Chinese companies. Many Chinese respondents were also concerned about the feasibility of requiring Chinese companies to make such disclosure and the reliability of the information that would be published.

Both Chinese and foreign stakeholders had positive views of the SSE's existing regulation on corporate social responsibility and mining rights acquisition and transfer. However, less than one-third of respondents felt that the current information on the SSE's Social Contribution Value Per Share (SCVPS) system and "transfer of mining rights" was useful. The majority of respondents stated that the requirements were difficult to understand, suggesting that the SSE should clarify and standardize these systems.

From the company and stakeholder studies in this report, it is clear that company reporting on payments is irregular and fragmented and that the SSE's conditions on disclosure do not always increase clarity and guidance. However, this report demonstrates that existing innovative provisions offer potential for improvements regarding transparency measures.

The key recommendation is that the SSE should review its existing sustainability disclosure requirements, especially targeted at the resource extractive industry. Ample scope exists for improving guidance on financial disclosure, including the definitions of information to be published, such as the Social Contribution Value Per Share.

This report also recommends the SSE to follow international best practice standards and require extractive companies to annually provide details on payments to domestic and host governments. The SSE could mandate resource extractive companies to annually report on payments to governments on a country and project level.

A revenue disclosure requirement would improve the image, functioning and attractiveness of the SSE, help reduce corruption, protect investment and enable Chinese companies to build better, more stable and more mutually beneficial relations with the communities they operate in (see Chapter Three on the economic importance of the extractive industry in China, and how the SSE would gain from requiring increased extractive industry payment disclosure).

The SSE has a great opportunity to change Chinese and international assumptions about the business and investment climate in China. If the SSE sets clear reporting requirements for extractive industry payments to governments, it will not only draw the admiration of investors and other stakeholders in the extractive industry, but will also improve the overall business and investment climate in China. Introducing a requirement for extractive companies to disclose payments made overseas would define the SSE as a leader among exchanges for extractive company listings.

2. Introduction

China's quest for extractive resources

China faces shortages in almost all energy and raw materials needed to fuel its high economic growth, particularly key commodities such as oil, copper, bauxite, uranium, aluminium, manganese, and iron ore.⁴ As a latecomer to the international markets, the country typically pursues investments in relatively new commodity sources, where it has encountered challenging political and operating environments. The country has built long-term trade linkages with Africa, Latin America, Russia, and other resource endowed regions by strengthening bilateral trade relations, awarding aid, and developing transport and communications infrastructure.⁵

China's "go-out" strategy, formally adopted in 2000, was the first signal that the Chinese government was prioritizing outward foreign direct investment (FDI). The policy prescribes Chinese state-owned companies to strengthen their international operations to improve resource allocation and enhance international competitiveness. In 2004, the National Development and Reform Commission (NDRC) and the Export-Import Bank of China (EXIM) released a statement to encourage overseas investment (and mergers and acquisitions) in specific areas such as resource exploration.⁶ Also, the State Council incentivized Chinese companies to enter overseas markets by granting financial and foreign exchange assistance.⁷

China's growing investments abroad are illustrated by China's growing FDI outflows over the last decade, which rose from US\$1.8 billion in 2004⁸ to US\$65.11 billion in 2011⁹. Chinese overseas investments exist in nearly 180 countries or territories.¹⁰ The final destination of Chinese outward FDI is sometimes difficult to determine because more than an estimated three quarters goes through tax havens such as the Cayman Islands and the British Virgin Islands.¹¹ A substantial amount of outward FDI into Hong Kong also flows back to China.¹²

China's state-owned resource extractive companies have been central to this international flow of investment. About US\$1 in every US\$7 of China's outward FDI stock is

reported to flow into the mining industry.¹³ At a national level, energy resource and mineral companies make up the majority of China's top ten companies, excluding banks, ranked by outward direct investment or foreign assets.¹⁴

Corruption in resource-rich countries

Chinese extractive companies face particular risks because the resources they extract often originate from corrupt and volatile regions. Angola – source of around one in every eight barrels of China's petroleum imports¹⁵ – exemplifies the particular risks and potential scale of corruption in the extractive sectors. A Chinese joint venture has purchased large stakes in major deepwater fields and the Chinese government has provided multi-billion dollar lines of credit, backed by oil, to the Angolan government.¹⁶ A Global Witness report from January 2012, entitled *Rigged: the Scramble for Africa's Oil, Gas and Minerals*, revealed that small and obscure companies in Angola who partnered with major international companies acted as fronts for government officials or their allies in resource deals.¹⁷ It is difficult to determine precisely how much oil revenue has been diverted without transparency of the payments made to the Angolan government coming from the extractive industries. However, the International Monetary Fund estimated that US\$32 billion in public funds went missing between 2007 and 2010.¹⁸

At the national level, Mr Xi Jinping, the newly appointed Chairman of the Chinese Communist Party, has spoken strongly about the risk corruption plays to China's national wellbeing and security. In his 15th November inaugural speech, he said that a top priority was fighting corruption. He later went on to say that it could "kill the Party and ruin the country".¹⁹

Improved disclosure for the resource extractive industries

There is growing international awareness of the need for greater transparency in the extractive industries as a vital first step towards tackling the resource curse and the corruption within the sector. Revenue disclosure can help deter corruption by enabling citizens to track payments to governments and where they end up. It also reduces the scope for officials to demand costly bribes

i Monetary values throughout the report are in US dollars using an International Monetary Fund exchange rate of ¥6.2804:US\$1, correct on 8th January 2013, unless stated otherwise.

and enables fairer competition between companies by helping to exclude secret payments for special access to resources. Additionally, revenue disclosure can help reduce the reputational and financial risk faced by companies should they be accused of bribery, embezzlement or fraud.²⁰ It also strengthens a company's 'social license to operate' – the confidence shown by a local community towards a company – by demonstrating the contribution the company makes to the state and local finances, reducing the likelihood of conflict. Where payments to governments are not disclosed, even companies paying substantial taxes may become targets for resentful populations, especially if revenues fail to trickle back to communities due to government corruption. In these cases, disclosure of payments by companies puts the onus back on to governments to account for revenues received.

A special role for the Shanghai Stock Exchange?

Financial markets have great transformational power to accelerate the transition towards more responsible and sustainable business practices and value creation. In particular, stock exchange listing requirements can affect the business practices of companies seeking to access capital from global retail and institutional investors.²¹ The Hong Kong stock exchange (HKEx) set an important global precedent when it required extractive companies to produce a one-off report on their payments to governments when listing in respect of taxes, royalties and other significant payments on a country-by-country basis.²² However, currently there are no specific regulations in Hong Kong or elsewhere in China concerning disclosure of ongoing payments made to foreign governments by listed oil, gas and mining companies.

In 2009, China's State Council declared that by 2020, Shanghai would establish itself as one of the world's pre-eminent international financial centres.²³ The China Securities Regulatory Commission (CSRC) has also announced it will deepen financial reforms and accelerate structural reorganization of the financial sector as a whole.²⁴ An important contributor to these developments is the Shanghai Stock Exchange (SSE).

Greater transparency in the SSE could help to promote a better business and investment environment for Chinese companies, enhance China's reputation abroad and promote international development. Disclosure requirements of the payments made to governments from resource extractive companies listed on the SSE would be in line with the aims of encouraging transparency and enabling investors to perform satisfactory risk assessments of stock portfolio.

Global Witness

Global Witness, a non-profit organization founded in 1993, has carried out investigations in many resource-rich countries in Africa and Asia, as well as research of extractive companies and banks based in the United States, Europe and other regions. The organization's work has revealed how, rather than benefiting a country's citizens, abundant timber, diamonds, minerals, oil and other natural resources can incentivize corruption, destabilize governments, and lead to war. Through investigations and advocacy, the organization seeks solutions to the 'resource curse' to prevent conflict and corruption and so that citizens of resource-rich countries can, hopefully, get a fairer share of their country's wealth.

Global Witness supports the implementation of anti-corruption and pro-transparency initiatives that change company and government behaviour so that natural resources contribute to development and poverty alleviation rather than conflict and corruption.

The organization's expertise is of wide relevance to policy makers, researchers and companies in China where concerns include the commercial and reputational risk faced by investments and also workers' risk of insecurity in unstable or violent countries. Global Witness is actively seeking links with relevant institutions within China, through the sharing of expert information and analysis and sustained dialogue. Global Witness is developing its outreach to Asian governments and hopes to establish a presence in the region in 2013.

For more information about Global Witness, please visit: www.globalwitness.org

Cooperation Global Witness - SynTao

In 2012, Global Witness commissioned the Chinese sustainability consultancy SynTao to perform a study on the reporting practice of large Chinese resource extractive companies with operations abroad and the views of Chinese and international stakeholders of the Chinese oil, gas and mining industry on international disclosure best practices.

SynTao Co., Ltd. is a leading Beijing-based consultancy promoting sustainability and responsibility in the Asian region. The company provides consulting, research and training services in Corporate Social Responsibility (CSR) and Socially Responsible Investment (SRI). SynTao has developed successful partnerships with a wide range of local and overseas organizations such as international and national corporations, government agencies, NGOs, academic institutions and media groups.

3. Best practices for the disclosure of payments to governments

What are payments to governments?

Governments grant companies the right to explore, develop and produce natural resources. In exchange, companies may pay tax, royalties, license fees and bonuses to the governments as compensation for the exploration, production and sale of those resources. Payments to governments should be agreed on in legally-binding contracts and openly reported on by governments and companies.

This chapter presents an overview of current best practice that the Shanghai Stock Exchange (SSE) could take into consideration when drafting detailed reporting requirements for its listed resource extractive industries.

Disclosure of payment details

Disclosure standards that require extractive companies to report on detailed aspects of payments to governments promote transparency and allow stakeholders to assess the scope, revenues and nature of exploration.

When discussing reporting payments to governments, the following aspects should be taken into account:

- **Disclosure of payment items:** i.e. what type of payments are being disclosed such as royalty payments, taxes, profits/dividends, commodity-based payments, signing bonuses, pipeline/transit tariffs, dividends, acreage fees, rental fees, and social development funds/community-based payments, infrastructure payments, etc.
- **Disclosure of payment levels:** i.e. at what level is disclosure taking place, e.g. government level transparency (separate disclosure for each government body such as federal government, regional government, local municipalities); country level transparency (separate disclosure for each country) or; project level transparency (activities governed by a license, concession or similar legal agreement).

- **Timing of disclosure on payments:** i.e. one-off (for instance at the time of the company's listing); annually (at the end of the fiscal year, together with the release of the annual financial report); or continuously (following each payment).
- **Whether there are disclosure exemptions:** no country exemptions of any kind should be allowed, as this would work in the opposite direction of the intention to promote disclosure. Corrupt governments in resource-rich countries would be incentivized to pass opacity laws outlawing disclosure, which would exclude some extractive companies meant to be covered from disclosure requirements from reporting critical information, and thereby undermine transparency.

Global initiatives

Various global voluntary and mandatory initiatives exist to promote greater financial transparency in the extractives sectors. Participants include governments, non-governmental organisations and companies.

Extractive Industries Transparency Initiative

The Extractive Industry Transparency Initiative (EITI) was launched in 2002 at the World Summit for Sustainable Development in Johannesburg to promote a global standard of revenue transparency. The initiative is a coalition of governments, companies, civil society groups, investors and international organizations that support improved governance in resource-rich countries through the full publication and verification of company payments and government revenues from oil, gas, and mining. It has become the most widely practiced payment disclosure system in the world for oil, gas and mineral extraction.

EITI's achievements so far include:

- 30 countries have produced EITI reports – including Iraq, Nigeria and Norway.
- More than 900 companies have disclosed a combined total of over US\$600 billion in payments.²⁵

- 18 countries are officially “Compliant Countries”²⁶ in the initiative – including Mongolia, which sent an estimated 92% of its total exports to China in 2011.²⁷
- 70 of the world’s largest oil, gas and mining companies have chosen to become EITI Supporting Companies, including Alcoa, ExxonMobil and ArcelorMittal.²⁸ There are not yet any official EITI Supporting Companies from China.

The EITI requires every implementing country to create its own national disclosure process, which is overseen by participants from the government, companies and national civil society. It is a voluntary system, but implementation of EITI must be consistent with the criteria below and there are checks to assess compliance²⁹:

1. Regular publication of all material oil, gas and mining payments by companies to governments (payments) and all material revenues received by governments from oil, gas and mining companies (revenues) to a wide audience in a publicly accessible, comprehensive and comprehensible manner.
2. Where such audits do not already exist, payments and revenues are the subject of a credible, independent audit, applying international auditing standards.

3. Payments and revenues are reconciled by a credible, independent administrator, applying international auditing standards. The administrator’s opinion of the reconciliation, including any discrepancies, is published.
4. This process is extended to all companies including state-owned enterprises.
5. Civil society is actively engaged as a participant in the design, monitoring and evaluation of this process and contributes towards public debate.
6. A public, financially sustainable work plan for all the above is developed by the host government, with assistance from the international financial institutions where required, including measurable targets, a timetable for implementation, and an assessment of potential capacity constraints.

In a number of countries, EITI reporting goes down to project-by-project reporting detail (including Chinese companies reporting at this level), this level of detail is not yet a requirement of the EITI. At the time of writing this is under review as the International Board of the EITI introduce new rules which may seek to update EITI to match mandatory requirements in the EU and US.

The World Bank and G8 have both provided formal and sustained support for EITI since 2003. In 2009, the leaders of the G20, of which China is a member,

Project-by-project reporting

Communities living close to resource extraction sites are often directly affected by them, and in some cases they are legally entitled to a percentage of the revenue generated by resource projects. Yet currently, citizens and local officials do not have access to financial information about projects established in their local area.

Royalties and other revenue payments are typically negotiated on a project-by-project basis. Having access to project-level data would allow investors to properly assess risk, governments to better monitor company compliance, and local communities to track who is gaining from particular resources. Conversely, if revenue information is aggregated at country level it would obscure often very large payments and be of limited use for improving transparency.

In recognition of this, Section 1504 of the US Dodd-Frank Act requires extractive companies to report the payments they make to governments that arise from each individual project they invest in (see p.10 for more details). This is known as ‘project-by-project’ reporting. The EU Transparency Directive is also expected to require project-by-project reporting (see p.11 for more details).

The US Securities and Exchange Commission provided clear guidance on how “project” is to be understood for the purposes of reporting under Section 1504. The SEC noted that the term is commonly understood within industry, and determined that “project” reporting should be linked to the contractual arrangements that define the relationship and payments made between companies and governments.

declared support for EITI, stating that “disclosure of payments and revenues ... empower(s) citizens and contributes to reducing poverty”.³⁰ Additionally, China has expressed its support for the UN General Assembly Resolution which emphasizes that all Member States should promote transparency.³¹ The EITI has stated that its reporting tool, which serves as an instrument to promote more stable conditions in supplier countries, is consistent with China’s non-interference policy.³²

Chinese companies operating in EITI compliant countries are known to have contributed data to EITI reports (see Table 1).

EITI reporting templates require the disclosure of payments that arise from individual resource projects in some countries in which Chinese extractive companies operate. In Indonesia for example, the companies must report payments that arise from each production-sharing contract. Petrochina and CNOOC participated in the multi-stakeholder process that resulted in this standard. In Zambia, where Chinese mining firms hold significant investments, EITI requires mining companies to report revenue payments that arise from each lease they operate.³³

For more information about the EITI, please visit the initiative’s website: www.eiti.org

Publish What You Pay

The Publish What You Pay coalition (PWYP) promotes greater transparency and accountability in the extractive industry and asks companies to “publish what you pay” and governments to “publish what you earn.” Specifically the coalition calls for programs in which companies report all payments for each country they operate on a project-by-project basis, including payments to local authorities, without any reporting exemptions, regardless of country or project type.³⁴

Mandatory and voluntary reporting requirements are seen as highly complementary, with mandatory requirements generating reporting in countries with very poor governance records that are unlikely to ever join a voluntary initiative like the EITI, and with EITI reporting adding additional data on government receipts of revenues to help close the gaps in transparency.

PWYP is also requesting mandatory transparency in extractive industry contracts and in license allocation procedures to bring these in line with best international practice, given that corruption takes place in other parts of the extractive ‘value chain’, beyond revenue payments made to governments.³⁵ Furthermore, PWYP recognizes that governments need to be accountable for how they spend their revenue in order to reduce

corruption and deliver revenue from natural resource extraction. This concern has led PWYP to encourage governments to “publish what you spend.”³⁶

The coalition is made up of over 600 organisations across 60 countries, with national affiliated coalitions in 31 of these. Global Witness and a collection of concerned NGOs established the PWYP coalition in 2002 following the launch of a report which documented the embezzlement of government revenue from Angola’s extractive industry during the preceding decade.³⁷ PWYP was also instrumental in founding and expanding the EITI.

For more information about PWYP, please visit the initiative’s website: www.publishwhatyoupay.org

The Global Reporting Initiative

The Global Reporting Initiative (GRI) is a non-profit organization that provides companies across many industries a structure to report on their sustainability efforts. A GRI report must focus on four key performance indicators of sustainability: economic, environmental, social and governance. GRI has a special report supplement for the mining and metals industry titled the Mining and Metals Sector Supplement (MMSS), established in 2005. On 29 February 2012, GRI introduced a new supplement for the oil and gas industry titled the Oil and Gas Sector Supplement (OGSS).³⁸ Commentary was added on the first economic indicator in both guidelines that oil and gas companies should report on payment to governments broken down by country. GRI does not require companies to file reports at any specific time or at any specific interval. Reporting is completely voluntary. Many companies release GRI reports annually or biennially.

MMSS and OGSS reports are comprehensive and focus on many aspects of business (such as environmental performance, labour practices and human rights). This is a major contrast to the other extractive industry evaluation regimes which have narrower focuses. GRI reports focus on many financial aspects of extractive companies. These aspects include reporting on:

- Significant financial assistance received from government;
- Percentage and total number of business units analyzed for risks related to corruption;
- Total value of financial and in-kind contributions to political parties, politicians, and related institutions by country.³⁹

Table 1: Overview of Chinese companies contributing data to an EITI country report

Country reporting under the EITI framework	Company (as stated in the EITI report)	Year
Afghanistan	MJAM MCC-JCL Aynak Minerals Company Ltd ⁱ	2008-10
Azerbaijan	Shengli Oil ⁱⁱ	2003-2007
Chad	CNPCI	2007-9
DR Congo	Congo Dongfang International Mining ⁱⁱⁱ	2008-9
Gabon	Sinopec	2006
Gabon	Sinosteel	2006
Gabon	Compagnie industrielle et commerciale des mines de Huazhou ^{iv}	2007-8
Iraq	China ZhenHua Oil Company	2009
Iraq	China National United Oil Corporation	2009
Iraq	Sinochem International Oil (London) Co. Ltd	2009
Kazakhstan	CNPC International (Buzachi) Inc	2005-2009
Kazakhstan	CNPC-Aktobemunaygas JSC (written as SNPS in 2006 report)	2005-2009
Kazakhstan	CNPC – Ai Dan Munay JS	2009
Liberia	China Union Investment (Liberia) Bong Mines Company Ltd	2009
Liberia	China Union (Hong Kong) Gold Investment	2009
Liberia	China Union Mining Corporation Limited	2010
Mauritania	CNPCI	2006
Mongolia	Chinhua MAK Nariin Sukhait ^v	2006-2010
Mongolia	Petro China Daqing Tamsag (Mongol) LLC / Petro China	2006-2010
Mongolia	Shin Shin LLC	2006-2010
Niger	CNPC – Niger Petroleum or CNPC International Bilma/Tenere	2005 - 9
Niger	China National Uranium	2007
Republic of the Congo	CNOOC	2007-2009
Republic of the Congo	CNOOC	2010
Zambia	Sino-Leach / Sino-metals Leach Zambia Ltd ^{vi}	2008-2009
Zambia	CNMC Luanshya Copper Mines plc	2009

i Joint venture includes China Metallurgical Construction Company and Jiangxi Copper Company Limited

ii Company controlled by Sinopec

iii Subsidiary of Zhejiang Huayou Cobalt Company Ltd

iv Subsidiary of CITIC

v Chinese and Mongolian joint venture, 50% held by Chin Hua Group of China and other 50% by Mongolian Gold MAK LLC.

vi Subsidiary of China Nonferrous Metal Mining (Group) Co. LTD

Disclaimer: EITI reports publish names of companies, including joint ventures. However, individual companies within a joint venture may not be discernable from the name. As a result, some Chinese-registered companies may not be included in the list above despite their participation in EITI.

If a company is stated as being included in the scope of an EITI country report, it is assumed that they contribute data unless explicitly stated otherwise.

International regulations

Listing rules of the Hong Kong Stock Exchange

In 2010 the Hong Kong Stock Exchange (HKEx) accepted new disclosure rules for extractive company listings, requiring applicants of the exchange to include in their listing application additional information on tax, royalty and other payments to host governments (country-by-country).

Specifically, the HKEx's new rules, announced after a two-month formal consultation process and several months of internal review, require disclosure of "material" information regarding⁴⁰:

- (a) project risks arising from environmental, social, and health and safety issues;
- (b) any non-governmental organisation impact on sustainability of mineral and/or exploration projects;
- (c) compliance with host country laws, regulations and permits, and payments made to host country governments in respect of taxes, royalties and other significant payments on a country by country basis;
- (d) sufficient funding plans for remediation, rehabilitation and closure and removal of facilities in a sustainable manner;
- (e) environmental liabilities of its projects or properties;
- (f) its historical experience of dealing with host country laws and practices, including management of differences between national and local practice;
- (g) its historical experience of dealing with concerns of local governments and communities on the sites of its mines, exploration properties, and relevant management arrangements; and
- (h) any claims that may exist over the land on which exploration or mining activity is being carried out, including any ancestral or native claims.⁴¹

Since the legislation was enacted, several extractive companies have listed on the HKEX, including CITIC Dameng Holdings Industries Ltd and China Gold International Resources Corp. Ltd. Companies that have several mines or agreements have typically reported on individual projects have disclosed information in a disaggregated form, on the basis of the following:

- mining licenses
- production-sharing agreements

- joint venture agreements
- significant ownership interest in extractive companies, where the subsidiary is engaged in extractive activities
- consortia.⁴²

United States: Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (2010)

While the EITI is a voluntary approach to establish revenue transparency in the extractive sector, section 1504 (or the 'Cardin-Lugar Amendment') of the US Dodd-Frank Wall Street Reform and Consumer Protection Act (2010) outlines the legal obligations requiring extractive companies to disclose payments to governments. Section 1504 was signed into law, along with the rest of the Dodd-Frank Act on 21 July 2010, by President Barack Obama. On 22 August 2012, the Securities and Exchange Commission voted on the final rules for implementation of the specific '1504' amendments requiring revenue disclosure.

Section 1504 requires extractive companies involved in commercially developing oil, gas and mineral resources (defined as "exploration, extraction, processing, export and other significant actions relating to oil, natural gas or minerals") to disclose the payments they make to the US and foreign governments that they operate in. Extractive companies should report their payments in publicly accessible yearly reports delivered to the SEC, beginning with fiscal years ending after 30 September 2013. This requirement applies to all publicly traded companies in the US regardless of whether they are based in the US or abroad. Companies include eight of the ten world's largest mining companies and 29 of the 32 largest internationally active oil companies.⁴³

Section 1504 requires extractive companies to disclose their payments to US and foreign governments on a country-by-country basis (i.e. the type and total amounts of payments made to each government) and project-by-project basis (i.e. the type and total amount of payments made for each project). Payments include taxes, royalties, fees (including license fees), production entitlements, bonuses (including signature bonuses), dividends, and infrastructure improvements that equal or exceed US\$100,000 during the most recent fiscal year, either as a single payment or a series of related payments.⁴⁴

The SEC's definition of project excluded more aggregated forms of reporting including reporting at a country by country level, geological basin or business reporting units internal to company structures, or definitions that refer to a project's materiality to a company. Instead SEC guidance outlines that "project" reporting is linked

to the “contractual arrangements” that define the relationship and payments made between companies and governments: “The contract defines the relationship and payment flows between the resource extraction issuer and the government, and therefore, we believe it generally provides a basis for determining the payments, and required payment disclosure, that would be associated with a particular ‘project’.”⁴⁵

China’s three big state-owned oil concerns – PetroChina (the principal holding company of CNPC), Sinopec and China National Offshore Oil Corporation (CNOOC) – are only partially state-owned. All have publicly listed shares in the US and will therefore have to comply with Section 1504. As a result, PetroChina will be required to disclose payments made to governments in the countries where it operates.

European Commission: Transparency Directive

On 25 October, 2011, the European Commission proposed a review of its Accounting Directive and the introduction of a new, but related, Transparency Directive. The Transparency Directive requires EU oil, gas, mining and timber companies to publish their payments to foreign governments. The European Parliamentary Legal Affairs Committee comprised of MEPs (Members of the European Parliament who are directly elected by EU citizens) was remitted with scrutinising proposed legislation on behalf of the Parliament and subsequently voted in September 2012 to include strong project-by-project reporting requirements to match US SEC rules. Following normal EU legislative procedure, the Parliament committee now takes their proposed version of the legislation into debate with the EU Council (made up of ministers from EU member states). The outcome of the negotiation between the two groups will determine the final version of the directive that is likely to pass into law during early 2013.

The EU Transparency Directive proposal is broader than Section 1504 in some regards, for example by including companies which are: extracting timber from primary forests; listed on European Union stock exchanges; and not listed in the EU but with headquarters in the region. Similar to Section 1504, the proposals include a requirement for extractive companies to report payments on a project-by-project basis.

As in Section 1504, various stakeholders have concerns regarding how the directive defines a “project” and if there are exceptions for certain countries. The definition of ‘project’ is still a matter of debate between Parliament and Council, with the Parliamentary Legal Affairs committee suggesting a definition based upon individual contracts from which fiscal terms with a government arise – in alignment with the SEC rules direction that projects should be based on contracts, while the Council suggest

much looser definitions including the ‘reporting units’ and geographical definitions that have been rejected by the SEC. Both Parliament’s Legal Affairs committee and the Publish What You coalition propose a definition in which projects are equivalent to “activities government by a single contract, license, lease, concession or similar legal agreement with a government upon which payment liabilities arise”.

While the Parliamentary Legal Affairs Committee, like the SEC, rejects exemptions in reporting which would offer loopholes for regimes to prevent disclosures, the European Council has requested that exemptions should be admitted only in the case of existing national laws that prohibit revenue disclosure. Again this is a matter of continuing debate between the two bodies, although exemptions are likely to be excluded from the EU Directive in order to create consistency with the US law which explicitly rejected them.

Overview

The disclosure standards cover a wide spectrum of payment reporting requirements (see Table 2).

Concerns

A number of concerns have been articulated by some stakeholders in the extractive sector, particularly companies and industry organizations. These concerns are listed below, as well as Global Witness’ response.⁴⁶

Disclosure threatens competitiveness

In the US context, companies and trade organisations such as the American Petroleum Institute have complained that revenue disclosure by US listed companies would give an unfair competitive advantage to companies who were not required to disclose payments.⁴⁷ However, extractive business success is not premised on secrecy, but on a host of other factors including technological assets and expertise, capital requirements and the fiscal terms that companies offer.⁴⁸

In addition, there is evidence that disclosure practices do not likely cause a competitive disadvantage. Successful companies which practise voluntary disclosure on a country-by-country basis for all countries of operation include Statoil Hydro (Norway), Newmont Mining (US), Talisman Energy (Canada) and Anglo Gold Ashanti (South Africa). Rio Tinto (UK-Australia) and AngloAmerican (UK) also disclose payments in a selection of countries where they operate. Not only have these companies succeeded in operating transparently, they have been able to disclose without suffering any negative externalities.

Table 2: Overview of payment disclosure standards for the resource extractive industries

	US Dodd Frank 1504	EU (in negotiation)	HKEx	EITI	GRI
Mandatory	√	√	√		
Voluntary				√	√
Payments to National Governments	√	√	√	√	√
Payments to Sub-National Governments	√	√			
Report payments for each project	√	√		TBC*	√
Exceptions for certain countries		TBC	X	Voluntary	
Clear Definition of “Project”	√	√		TBC*	
Spending on Locally- Based Suppliers	√				√
Primary Forest Logging		√			
Report on Payments related to Transport and Export					√
Report payments received by governments				√	

*not required but takes place in a number of countries. May be a requirement through new EITI subject to agreement by May 2013

Disclosure on payments to governments is too expensive

The US SEC rules recognise that the Dodd-Frank 1504 rules increase costs to companies. However, estimates made by both the SEC and the EU undermine company estimates of costs of reporting and reject the idea that the cost would outweigh the benefits. It is widely assumed that companies and their subsidiaries already record information on payment reporting for internal accounting purposes. Companies would need to repackage internal disaggregated data on payments to governments to make it suitable for release in the companies’ financial statements. Also, most companies are already involved in some sort of public disclosure practices, either through accounting provisions of national anti-bribery statutes or through the requirements of EITI.

Companies may fail to win contracts from countries who do not want them to disclose revenues

A review of *Upstream* magazine, which reports on deals in the oil and gas industry, from September 2011 to February 2012, reveals that there were numerous bidding rounds for oil and gas exploration rights around the world during the period and not a single report of any company

being excluded because of concerns about transparency.⁴⁹ The success of the successful companies was instead judged to be based on technological advantage, fiscal terms offered, access to capital, the efficiency and management of their business and their track record. Lord Browne, the former head of BP, has also written to the Financial Times confirming that he does not believe financial disclosure creates competitive harm.⁵⁰

Disclosure will lead to publication of commercially sensitive information

Information disclosed under Section 1504 and the future EU Directive does not allow other companies to discover the bidding strategies of companies nor does the information include future transactions and trade secrets. Some oil, gas and mining contracts containing this information as well as more sensitive information can be purchased on industry specific websites and general contract websites such as the Barrows Company and Alexander’s Gas and Oil Connections.⁵¹ More sensitive information within the oil, gas and mining industries such as geological data, costs or profits, are not covered by Section 1504 nor by the EU directive.

Project-by-project reporting is not commercially sensitive because it cannot be used to deduce a company’s contract terms, expected reserves, operating

costs, or future plans without a lot of other information that is not publicly available. Also, information about payment terms only gives insight about a company's performance over a very short timeframe, as prices, political situations, and the knowledge about geological formations change monthly. Therefore, any potential damage to a company's competitive position would be minimized by the lapse of time between the making of payments and the timing of publication.

National laws and contracts might prohibit disclosure

A concern that criminal legislation within countries could prevent companies from disclosing revenue payments made to governments has been raised by companies opposing transparency laws in the US and EU who have been demanding 'exemptions' from reporting in such countries. In deliberating on the final implementation rules for Dodd Frank 1504 however, the SEC found insufficient evidence to justify any exemptions and judged they might result in corrupt officials in resource-rich countries being incentivized to pass opacity laws, outlawing disclosure and thus undermining the whole purpose of the transparency initiative.

A global survey of over 150 resource extraction contracts by the Revenue Watch Institute and Columbia University School of Law concluded that contracts usually state that the parties may make disclosures under any law to which the party is subject.⁵² Some industry representatives cite Angola, Cameroon, China and Qatar regarding an alleged need for disclosure exemptions, although no evidence was actually cited to prove this point when companies were called to provide evidence.⁵³ Indeed, Brazilian oil company Petrobras, which operates in both Angola and China, informed the SEC: 'We are active in 29 countries outside of Brazil and we are not aware of such a prohibition [against payment disclosure] in any of those countries.'⁵⁴

Focus on China

For years, China has been among the world's fastest growing economies, with real annual gross domestic product (GDP) averaging nearly 10% through 2011. As China's economy continues to develop, the country has quickly become one of the world's largest consumers and importers of extractive resources. In parallel, Chinese energy resource and mineral companies have steadily developed activities overseas, establishing a strong presence worldwide. This has automatically increased global attention on disclosure practices by Chinese companies particularly in relation to the management of risks such as rent-seeking and corruption in the mining, oil and gas industries.

Chinese reporting standards

China has yet to craft a complete system of laws and regulations for companies to regulate fair conduct or disclosure regarding overseas investment are limited and fragmented.

Multiple government departments are involved in the process of administration and supervision of overseas investments. Depending on the scale and nature of investment, Chinese government institutions that must approve an overseas project include the State Council, the Ministry of Commerce (MOFCOM), National Development and Reform Commission (NDRC), Ministry of Finance, State Administration of Foreign Exchange (SAFE), State-owned Assets Supervision and Administration Commission (SASAC), as well as the China Export-Import (Exim) Bank and the China Development Bank.⁵⁵

The most specific requirement can be found in the *Administrative Regulation on Contracting Foreign Projects (2008)* issued by the State Council that states that the company, and any people involved, shall be fined or the certificate shall be revoked when the project is obtained as a result of offering an unfair low price, illegal bidding or acts of bribery.⁵⁶

However, most articles related to the impacts of company behaviour overseas tend to be general and are not meant to scrutinize companies' activities. For instance, the *Tentative Administrative Procedures on Overseas Investment by State-owned Enterprises (2012)* issued by SASAC only emphasizes that state-owned companies shall abide by the laws and regulation and respect local customs of the host country.⁵⁷

China does not have specific law on domestic or overseas corrupt practices. All anti-corruption measures are described in the country's *Criminal Law* and *Anti-Unfair Competition Law*. In 2011, China made an amendment to the *Criminal Law*, providing sanctions to domestic companies if any money or property was offered to any foreign party performing official duties or officials of international public organizations.⁵⁸

Reporting for the extractive industries

In 1998, the State Council issued the *Measures for the Administration of Transfer of Mineral Exploration Right and Mining Right* to guide domestic mining rights transfer activities, but this document did not include a disclosure requirement.⁵⁹ In 2012, the Chinese Ministry of Land and Resources issued a pilot version for a revised guideline on mining rights transfers, requiring transfers to be carried out on a designated trading platform and provide full disclosure of bidders and transaction price.⁶⁰

Articles aiming specifically for disclosure in the resource extractive industries are included in the country's reporting regime. The China Securities Regulatory Commission (CSRC) requires public companies to disclose on its accounting practices, estimates of oil and gas assets, depletion, license cost, the evaluation standard for its reserves, and list the balance and accrual and decrease of oil and gas assets.⁶¹

In 2006, the Ministry of Finance issued the progressive *Accounting Standard for Business Enterprises No.27 -- Extraction of petroleum and natural gas*, providing specific data disclosure requirements to companies' financial statement on:

1. The beginning and the end year balance of domestic and overseas oil and gas reserves.
2. The total amount of all disbursements incurred in the current period in order to obtain the rights and interests of domestic and overseas mining areas, and for oil and gas exploration as well as their development.
3. The original book value of the rights and interests of the proved mining areas, wells and relevant facilities, the accumulative depletion amounts and the accumulative amounts of the impairment provisions as well as their calculation methods.
4. The original book value of the auxiliary equipment and facilities for the oil and gas exploitation activities, the accumulative depreciation amounts and the accumulative amounts of the impairment provisions as well as their calculation methods.

Following these general requirements, the Shanghai Stock Exchange and the Shenzhen Stock Exchange (SZSE) respectively issued their own guidelines for listed extractive companies in 2008.⁶² The two similar guidelines give detailed requirements on information disclosure regarding the obtaining and transfer process of exploration and mining rights. SSE's guideline includes a paragraph on acquisition and transfer of mining right overseas, requiring listed companies to provide evidence that activities are in line with the laws and regulations of the host country.

Chinese companies under scrutiny

Despite China's requirements on corporate reporting, the share prices of Chinese companies have recently been rocked by a series of accounting scandals both at home and abroad. In the last year, numerous Chinese companies have been exposed for possessing weak internal control over financial reporting and corporate

governance structures, which has sparked some doubt about the quality of corporate reporting in China.⁶³ Between March to June 2011 alone, more than 20 Chinese firms were suspended from trading or were delisted on U.S. exchanges for alleged financial fraud.⁶⁴

Several Chinese companies have entered the United States' stock market through reverse takeovers or mergers – a legal procedure whereby a Chinese company, with all its operations abroad, merges with an existing publicly traded US shell company and eventually raises money by selling shares to American investors. The non-listed company thereby bypasses the regulatory scrutiny process of a traditional initial public offering (IPO). The process is considered to bear notable risk as overseas regulators feel they have no way of reviewing the audit work done in China.⁶⁵

Chinese companies that entered overseas markets through traditional IPOs have come under particular scrutiny. Sino-Forest, an operator of forest plantations, filed for bankruptcy protection in Canada in March 2012, following the release of a negative research report voicing accusations of fraud and overstating of assets. Trading of the stock was suspended.⁶⁶

There are also some recent examples of Chinese companies not having their accounts independently audited by a registered auditor. In 2011, Deloitte's Shanghai branch resigned as the auditor of Longtop Financial Technologies (financial software provider) after uncovering numerous improprieties.⁶⁷ In March 2012, Deloitte resigned as auditor of two Hong Kong-listed Chinese companies, Boshiwa International (manufacturer of children clothing) and Daqing Dairy Holdings (producer of milk formula). The International Accounting Bulletin reported that Deloitte had not been satisfied with Boshiwa's response to questions about certain transactions.⁶⁸

Chinese accounting standards

A new Western-oriented set of Accounting Standards for Business Enterprises or Chinese Accounting Standards (CAS) came into effect in China in January 2007.⁶⁹ Dual-listed Chinese companies often report both according to CAS and the International Financial Reporting Standards (IFRS). While CAS is converging more and more with the IFRS, there is still a distinction between the two systems, especially regarding how they are interpreted and implemented.⁷⁰

China is known to suffer from shortages in skilled accountants and auditors, poor implementation of accounting standards, and a lack of enforcement of these accounting standards.⁷¹ These factors may slow down the development of corporate disclosure and

increase the risk of investors missing out on information regarding companies operations, especially overseas.

Shanghai Stock Exchange

A poor reputation in audit practices may affect the prospects of Chinese companies listing overseas as well as the influx of investment to stock exchanges in general. Therefore, improvements in corporate disclosure can directly improve investor confidence in Chinese mainland listed stocks.

Above all, it is China's stock exchanges – Shanghai Stock Exchange, Shenzhen Stock Exchange, Hong Kong Stock Exchange – that can play an important role in enabling shareholders to better manage risk and encourage companies to further improve reporting. This is particularly true for oil, mining and gas companies that operate in locations that may harbour higher equity risks and could therefore benefit from greater transparency.

The Shanghai Stock Exchange (SSE) is widely recognized for its efforts to promote corporate reporting and the development of sustainable economic growth. Initiatives such as the *Shanghai CSR Notice*, the *Shanghai Environmental Disclosure Guidelines*, and the *Guidelines for extractive companies* with operations abroad were well received by the investor community.⁷²

Promoting disclosure

Enhanced disclosure on payments made to host governments would allow investors and the public to better assess and understand the financial risks associated with resource extraction companies and the value that these companies create for China as a whole. Such measures coincide with the SSE's aim to make companies demonstrate their 'social contribution' to a harmonious society.

Social contribution per share

The term "social contribution value per share" (SCVPS) was first introduced in the Environmental Disclosure Guidelines published by the SSE in 2008. On the basis of earnings per share created for shareholders, the added value created for society is calculated by adding tax revenues created for the State, salary paid to employees, loan interest paid to creditors including banks, donations and other value for stakeholders, and deducting social costs from environmental pollution or other factors.⁷³ The social contribution value per share value can include payments made overseas as well as in mainland China. However, it is hard to tell whether companies integrate international costs into their SCVPS values because of the current opacity around how the figures are calculated.

In theory, the social contribution per share calculations helps the public to better understand the value created by the company for its shareholders, employees, customers, creditors, communities and the society at large. Companies are encouraged by SSE to disclose their social contribution per share in an annual sustainability report. Page 18 provides further analysis of the methodology used to create the SCVPS value and its usefulness.

Mineral Right Disclosure

The Shanghai Stock Exchange issued regulations in 2008, entitled "No.18 Format Instruction on Temporary Announcements of Listed Companies", requiring listed companies to disclose information regarding the acquisitions and transfer of their mineral rights.⁷⁴ Details set out in the instructions include whether companies have obtained exploration or mining licenses, whether they have the necessary project and environmental protection approvals as well as setting out industry standard information regarding the project's value such as recoverable reserves and how long the mineral reserves would last.

4. Company Assessments

This chapter takes a closer look at the financial disclosure and information on asset ownership of major Chinese resource extraction companies. The fifteen largest companies in terms of revenue, as ranked by the 2011 China Fortune 500,⁷⁵ that are listed on the SSE and operate in the overseas resource extractive industries (or in one of the industries that are closely connected to the exploration, manufacturing and sale of oil, gas and mining) were selected to be studied for the purpose of this report.

The corporate communications of all 15 companies, such as the annual reports and sustainability reports released for 2010 and 2011, were analysed based on a best-practice standard that includes the key disclosure items for the resource extractive industry according to international disclosure regulations and guidance. The benchmark standard assesses the level of disclosure of each company, including payments made to the Chinese government and host governments, transfer of mining rights, the scale of overseas operations and revenue and social contribution value per share (SCVPS) (see page xx).

Indicators used in benchmark analysis of disclosure of Chinese companies 2010/2011

Domestic Chinese market

- Social contribution value per share (not part of international disclosure standards)
- Level of disclosure
- Payments to domestic (local) government (taxes, royalties, license fee, bonuses etc)

Overseas markets

- Accounting standards
- Operations overseas
- Revenues overseas
- Payments to national host governments
- Income tax (share or amount)
- Transfer of mining rights
- Payments to (local-level) host governments (taxes, royalties, license fee, bonuses etc)

General findings

Nearly every company examined in this study applied a different approach to how they presented data on payments to governments. A few companies reported country specific information by highlighting a small and seemingly unsystematic number of payments, while others did not even reveal the location of any of their overseas operations.

Certain common characteristics of disclosure, however, were shared by all 15 companies⁷⁶:

1. Fragmented reporting

The data disclosed by companies selected for this study on payments to host governments and transfer of mining rights was found to be fragmented and irregular (see Annex 1, available online). It was only possible to compare the results of the company disclosures in general terms as all companies tend to disclose a different list of tax items, depending on type of project operation and sector categorization. In practice, companies reported only on the most important general taxes and taxes paid at a national level.

Overall, PetroChina, Zijin Mining, Maanshan Iron and Steel, China Oilfield Services and Yanzhou Coal Mining showed most openness about payments to governments in connection to overseas operations as they have disclosed either separate or aggregated figures of the taxes they paid to overseas governments. They set a cautious example for other Chinese companies on how to report beyond basic disclosure requirements (please refer to company profiles below).

In addition to disclosure in their annual reports, PetroChina and Zijin Mining reported on individual projects and detailed specific aspects of their investments on their company's group websites.

2. Extractive Industry Transparency Initiative data not reflected in company reports

China's two biggest extractive companies in terms of market capitalization, China National Petroleum Corporation (CNPC), the parent group of PetroChina, and Sinopec have been involved with the Extractive Industries Transparency Initiative (EITI) by contributing

to EITI country reports. However, data disclosed to EITI could not be traced back to any of the reports released by the two companies individually. For example, the Nigerian and Iraqi EITI reports listed payments made by CNPC to each of the host governments, but neither CNPC nor PetroChina re-published this data, or mentioned its participation in the EITI, in its own reports.

3. Improved reporting with overseas listings

There seems to be a strong relationship between a company's additional stock exchange listing and the level of transparency it exercised. A company listed in Hong Kong, New York or London, in addition to the SSE, is automatically subject to additional reporting requirements that result in slightly increased transparency on overseas operations. Of the 15 companies examined in this study, ten companies had an additional listing on the Hong Kong Stock Exchange (HKEx), four companies were listed on the New York Stock Exchange (NYSE), and one company was listed on the London Stock Exchange (LSE) (See Table 3).

When a company is listed on the HKEx or abroad, most companies start reporting according to the widely used International Financial Reporting Standards (IFRS), which is released by the International Accounting Standards Board (IASB). All companies listed on the SSE and the

HKEx reported according to IFRS in 2010 and 2011, except for Maanshan Iron & Steel and Zijin Mining, which reported according to Chinese Accounting Standards (CAS).⁷⁷ Notably, in Zijin Mining's 2011 annual report, financial data between 2007 and 2009 were reported according to IFRS, but figures in 2010 and 2011 shifted to CAS. Overseas information, if any, was found in the 'Segment report' of the company's financial reports.

4. Better quality reporting on tax payments than other items

Companies in this study only disclosed on tax related items rather than additional items such as licence fees, royalties and bonuses. When analysing disclosure for the domestic market, most companies reported on common tax items such as business, consumption, educational surcharge and city maintenance and construction. The disclosure for other tax items varied according to industry and some taxes were paid only to local provincial governments (see table 4). For small value payments, some companies just provided a cumulative number under the item "others" without details on individual tax items. Often tax information was provided as a percentage take by the government rather than an actual amount.

When looking at the companies that report according to IFRS, there was slightly more similarity in reporting on tax

Table 3: Overview company selection listed on SSE

Company listed on SSE	HKEx	NYSE	LSE	Report according to CAS/IFRS
Aluminum Corporation of China	√	√		CAS and IFRS
Baoshan Iron and Steel				CAS
Baotou Steel				CAS
China Coal Energy	√			CAS and IFRS
China Oilfield Services	√			CAS and IFRS
Gan Su Jiu Iron and Steel				CAS
Jiangxi Copper	√			CAS and IFRS
Maanshan Iron & Steel	√			CAS
PetroChina	√	√		CAS and IFRS
Shanxi Coal International				CAS
Shenhua Energy	√			CAS and IFRS
Sinopec	√	√	√	CAS and IFRS
Wuhan Iron and Steel				CAS
Yanzhou Coal Mining	√	√		CAS and IFRS
Zijin Mining	√			CAS (CAS and IFRS before 2010)

Table 4: Major Chinese domestic taxes related to the oil, gas and mining industry

Tax Item	Law	Applies to
Resource tax	Provisional Regulations on Resource Tax of the People's Republic of China (2008)	Oil, gas and mining enterprises
Mineral resource compensation fee	Administrative Measures of Mineral Resources Compensation Fee (1994). Notice of Collection of Mineral Resources Compensation Fee of Sino-Foreign Petroleum Resources (2012)	Oil, gas and mining enterprises
Exploration license fee	Measures for the Area Registration Administration of Mineral Resources Exploration and Survey (1998)	Oil, gas and mining enterprises
Production right usage fee	Measures for the Registration Administration of Mineral Resource Exploration (1998)	Oil, gas and mining enterprises
Special oil income levy	Administrative Measures of Special Oil Income Levy (2006)	Oil enterprises
Coal sustainable development fund	Administrative Measures of Coal Sustainable Development Fund of Shanxi Province (2007)	Coal producing enterprises located in Shanxi province
Water resource compensation fee	Administrative Measures of Water Resource Compensation Fee of Shanxi Province (1996)	Coal producing enterprises located in Shanxi province

payments. In this situation, companies specifically revealed the locations of operations overseas, sometimes even disclosing the share of income tax paid to host governments. Only three companies (PetroChina, Maanshan Iron & Steel and China Oilfield Services) made a distinction between domestic income tax and overseas income tax paid. PetroChina and China Oilfield Services also disclosed an aggregated amount of overseas tax other than income tax.

5. Social contribution value per share (SCVPS)

Voluntary disclosure on social contribution value per share (SCVPS) is an initiative the SSE launched in 2008, and one of the few reporting items that provides stakeholders with an insight of companies' impact on society. Since its introduction, a growing number of companies have reported a SCVPS score. The proportion of disclosures on SCVPS seems to remain stable, although the number of companies releasing CSR reports is rapidly growing. For 2011, only five of the 15 companies studied disclosed a SCVPS score.⁷⁸

The SSE features a Social Responsibility Index ranked according to SCVPS, encouraging companies to continue to report the score. However, the transparency of the SCVPS score could benefit from some improvements (see box below). At this point, it is not clear how items in the formula are calculated. For instance, SSE defines social cost as the amount that arises from environmental pollution and other negative factors. However, the question remains how this amount is calculated by companies themselves.

Most companies choose to include fines that have been paid for violations of environmental pollution. However, there are many other social costs that could be included in the calculation such as direct economic loss caused by pollution and environmental recovery expenses. The SSE also doesn't require a third party to verify the final score by a company.

Although SCVPS calculations seem to remain broadly consistent by individual companies for 2010 and 2011, they do not seem in any way comparable between

Formula for social contribution per share

Social contribution value per share (SCVPS) =

$$\frac{\text{earnings} + \text{tax payment} + \text{salary to employees} + \text{interest expenses} + \text{donation} - \text{social cost}}{\text{total number of shares}}$$

companies (even those in the same basic industry). This makes its utility debatable and is an issue that could be significantly improved with better guidance.

Companies did not discuss the transfer of mining rights in their annual reports with respect to the 2008 instruction.

Company profiles

In the following sections, each company is described by the nature of its core activities, its listing history and performance and its disclosure practices regarding overseas operations for the financial year 2010 and 2011.⁷⁹

The profiles do not look at transparency beyond payment disclosure. For instance, corporate environmental pollution is an important issue but remains outside of this report's remit.

All 15 companies mentioned in this report received a letter from Global Witness (in Mandarin) notifying them of the upcoming launch of the joint research project. Each company was informed of the key findings regarding its own level of disclosure of payments and invited to provide feedback before the release of the report. In total, four companies chose to send in a response. A summary of the responses from Sinopec, Yanzhou Coal, Baoshan Iron and Steel and China Coal Energy are included in boxes within the respective company sections below.

Aluminium Corporation of China

Key findings:

- Disclosure on total overseas revenues
- Disclosure of percentage of income tax paid in Australia and Hong Kong

Aluminium Corporation of China Limited (CHALCO), a subsidiary of the Chinese state-owned company Aluminium Corporation of China (CHINALCO), is an aluminium company and the world's fourth largest aluminium producer as of 2011, with an output of 3.13 million tons of aluminium.⁸⁰

CHALCO was listed on the SSE (SSE: 601600) material sector (manufacturing-metal category according to CSRC) in 2007 and the HKEx (SEHK: 260) and NYSE (NYSE: ACH) in 2001. The company's turnover showed an increase of 20% between 2010 and 2011, as well as showing a slight increase in total assets. CHALCO's market capitalization was US\$12.7 billion by April 2012.

CHALCO disclosed the percentage of income tax paid in Australia (30%) and Hong Kong (16.5%) in 2010 and 2011. The company's overseas revenues dramatically increased between 2010 (US\$35,826) and 2011 (US\$353 million) but the corporate communications do not comment on payments to governments. CHALCO's parent company CHINALCO disclosed the locations of its overseas subsidiaries in its corporate social responsibility report.⁸¹

Baoshan Iron & Steel

Key findings:

- Disclosure of overseas subsidiaries' profiles
- Disclosure on total overseas revenue

Baoshan Iron & Steel Company Limited (Baoshan), a wholly owned subsidiary of Shanghai Baosteel Group Corporation (Baosteel), is an iron and steel company. Baosteel is the world's third largest steel producer by production.⁸²

Baoshan listed on the SSE (SSE: 600019) material sector (manufacturing-metal of CSRC) in 2000. The company's turnover increased by 10% between 2010 (US\$32.19 billion) and 2011 (US\$35.49 billion). As of end 2011, Baoshan's market capitalization was US\$13.62 billion⁸³. In March 2012, the company posted its lowest quarterly profit in more than two years amid high iron ore prices and slowing demand from automakers and builders.⁸⁴ The company's SCVPS in 2011 was US\$0.33.

Baoshan disclosed the profiles of its overseas subsidiaries in its corporate communications. Location, registered capital asset, and business scope information was available for each subsidiary in the United States, Japan, Germany, Singapore, Hong Kong and Brazil. The company reported an increase of 19% on its overseas revenues between 2010 (US\$3.18 billion) and 2011 (US\$3.8 billion) but did not comment on payments to governments.

Response to SynTao -Global Witness findings

Baoshan Iron and Steel stated that, because all overseas extractive operations are carried out by the parent group, Baosteel Group, it is not the responsibility of the listed company to report on taxes paid by the group.

Regarding the activities of its subsidiaries abroad, the company said that its reporting meets the current disclosure requirements set by the SSE.

Baoshan Iron and Steel said that if the SSE starts requiring companies to increase disclosure on overseas payments, the company would report on these items.

Baotou Steel

Key findings:

- Disclosure on total export revenue

Inner Mongolia Baotou Steel Union Company Limited (Baotou Steel), a listed subsidiary of state-owned enterprise Baotou Iron and Steel Group (Baogang Group), is engaged in the steel industry. The company provides various steel products such as steel pipes, steel plates, and steel profiles.⁸⁵

The company is located in the large-scale industrial zone of Baotou, the largest rare earth industrial base in China, also known for its production of iron and steel, machinery, non-ferrous metals, and textiles. The company also operates a rare earth mine that produces niobium and thorium.⁸⁶

Baotou Steel was listed on the SSE (SSE: 600010) in 1997. The SSE categorizes the company in the Material Sector Index. The CSRC qualifies Baotou Steel as part of the manufacturing-metal industry. In February 2012, the company announced that its pre-tax profits in 2011 surged over 66% to US\$102.86 million. The company's revenues hit US\$6.82 billion in 2011, and as of April 2012, the company's market capitalization was US\$5.8 billion.⁸⁷

The company has sales branches but not extractive operations in Japan and the US. Its revenue streams for export totalled US\$0.42 million in 2010, and US\$0.59 million in 2011. The company did not disclose any data with respect to its overseas activities.

China Coal Energy

Key findings:

- Disclosure on aggregate overseas revenue for Asia Pacific area and other overseas markets
- Payment of 30% income tax to the Australian government

China Coal Energy Company Limited (China Coal Energy) is the second largest coal enterprise in China and the largest coal exporter in terms of volume and manufacturer of coal mining equipment in China. Its major businesses include coal production and

trading, coal chemical and coal mining equipment manufacturing and power generation.

China Coal Energy was established by China National Coal Group Corporation as a joint stock limited company in 2006. It was listed on HKEx (SEHK: 1898) in 2006 and in the energy sector (CSRC category: extractive industry) of the SSE (SSE: 601898) in 2008. The market value of the company was US\$18.38 billion in April 2012.⁸⁸ The company's score of SCVPS was US\$0.39 in 2011.

In 2010, a subsidiary of China Coal Group acquired a 51% stake in the Columboola mining area in Queensland, Australia, and it has been developing thermal coal jointly with Australian MetroCoal Company in the Surat Basin in Australia.⁸⁹ China Coal Energy paid 30% of its revenue as income tax to the Australian government in 2011. The company disclosed the cumulative revenue it gained in Asia Pacific (US\$159 million) and other overseas markets (US\$0.86 million) in 2011.

Response to SynTao -Global Witness findings

China Coal Energy confirmed the research findings above and emphasized that it strictly follows the requirements of the stock exchanges it is listed on – the SSE and the HKEx.

China Coal Energy said that they want to learn more about the conclusions of the study and verify the sources utilized in the report. The company was interested in better understanding its level of disclosure in comparison to other companies studied in the report.

China Oilfield Services

Key findings:

- Country by country disclosure of income tax payments' rate
- Disclosure of total overseas revenue
- Disclosure of total overseas income tax

China Oilfield Services (COSL), a majority-owned subsidiary of the Chinese state-owned China National Offshore Oil Corporation (CNOOC) Group, provides services in the offshore market, covering each phase of offshore oil and gas exploration, development and production. COSL is China's largest oilfield service provider and has four core business segments:

geophysical services, drilling services, well services, marine support and transportation services. COSL possesses the largest fleet of offshore oilfield services facilities in China.⁹⁰

COSL has been listed on the HKEx (SEHK: 2883) since 2002, and on the SSE (SSE: 601808) energy sector (extractive company by CSRC's classification) since 2007. Its sister company, CNOOC Limited, is listed on the stock exchanges of Shenzhen and Hong Kong. As of April 2012, COSL's market capitalization was US\$11.21 billion.⁹¹ The proportion of its revenue generated overseas is predicted to rise from under 2% in 2002 to 40% by 2015.⁹²

COSL's 2010 and 2011 corporate communications provide a relatively high level of disclosure. In addition to its domestic payments in China, the company reports on income tax to host countries (Table 5).

The country-by-country disclosure on income tax payments is remarkable as none of the other companies in this study have disclosed the payments in such detail. Although the company has not disclosed the actual amounts paid, it did state its overseas revenues for 2010 (US\$686 million) and 2011 (US\$823 million). Notably, the company also provided the total amounts for "other overseas taxes payable"; "overseas income tax paid"; "current overseas income tax" and "deferred overseas income tax" for 2010 and 2011.

Gan Su Jiu Iron & Steel

Key findings:

- No disclosure on any overseas financial information in its annual reports

Gan Su Jiu Steel Group Hong Xing Iron and Steel Company Limited ("Gan Su Jiu"), the largest steelmaker in terms of volume in China's northwest, is predominately engaged in mining and manufacturing of iron and steel products. The company was listed on the SSE (SSE: 600307) in the material sector (manufacturing – metal industry by CSRC categorization) in 2000. The market value of the company was US\$2.13 billion in December 2012.⁹³

Gan Su Jiu sells its products (and is not involved in resource extraction) in Japan, South Korea and Indonesia according to its website, and no export information can be found in its annual reports. In 2008, Jiuquan Iron & Steel (Group) Co., Ltd (JISCO) – parent company of Gan Su Jiu – formed a partnership with a Kazakhstani mining company to increase its steel supply. JISCO committed US\$4.78 billion to take a majority stake from a Dutch company to mine in Kazakhstan for iron ore.⁹⁴ JISCO did not disclose any overseas financial information in its company communications.

Table 5: Tax payments and requirements to host countries disclosed by COSL

Country	EITI status (correct as of December 2012)	Income tax 2010	Income tax 2011
Indonesia	Candidate country	25%	25%
Libya	-	borne by customer	borne by customer
Australia	-	30%	30%
Mexico	-	30% or business flat tax at 17.5%	30% or business flat tax at 17.5%
Myanmar	-	3.5%	4%
Papua New Guinea	-	-	borne by customer
Norway	Compliant country	28%	28%
Dubai	-	0%	0%
Iran	-	borne by customer	borne by customer
Saudi Arabia	-	borne by customer	borne by customer
Iraq	Compliant country	-	35%
United Kingdom	-	-	28%

Jiangxi Copper

Key findings:

- Disclosure of total revenue overseas and revenue separately disclosed for specific countries
- Disclosure of the amount of income tax paid in Hong Kong

Jiangxi Copper Company Limited (Jiangxi Copper) is a Sino-foreign joint stock limited company incorporated in 1997 and is the largest copper cathode producer in China according to volume of production. The company's business covers the exploration, mining, smelting, and processing of non-ferrous metals such as copper, gold and silver.

Jiangxi Copper was founded in 1979 in Guixi City, the center of the Chinese copper industry. The company was listed on the HKEx (SEHK: 0358) in 1997 and on the SSE (SSE: 600362) in 2002. Jiangxi Copper is in the "material" sector of the SSE index, and in the manufacturing-metal of CSRC's category. The market capitalization of the company was US\$11.92 billion in April 2012.⁹⁵ The company's SCVPS was US\$0.62 in 2011.

In its 2010 annual report Jiangxi Copper disclosed the revenue it gained overseas as a total as well as specific revenue in Hong Kong and Taiwan. In its 2011 annual report, disclosed the same items as well as adding the specific revenue in the Netherlands.⁹⁶ Jiangxi Copper disclosed the 16.5% income tax it paid in Hong Kong (US\$0.92 million in 2010, US\$0.44 million in 2011).

In 2008, Jiangxi Copper and China Minmetals acquired all shares of Northern Peru Copper.⁹⁷ Subsequently, it was reported that the companies would invest US\$2.5 billion in the project.⁹⁸

Jiangxi Copper and China Metallurgical Group Corporation wholly own the Aynak Mine project in Afghanistan, with 25% and 75% ownership respectively. The project has been delayed because of nearby ruins of historic Buddhist monasteries in 2012, which would need to be excavated before Jiangxi Copper can begin mining.⁹⁹ In the "Management Discussion and Analysis" section of the 2011 Annual Report, the company reported that no earnings were realised yet as the projects were still under construction.¹⁰⁰

Maanshan Iron and Steel Ltd

Key findings:

- Disclosure of total overseas revenue
- Disclosure of income tax paid to Hong Kong and an aggregated amount of all the other overseas countries

Maanshan Iron and Steel Company Limited (Maanshan Steel, ESHK: 0323) is the ninth largest Chinese steel producer by volume¹⁰¹ and one of the largest Chinese iron and steel producers by volume on the SSE (SSE: 600808) material sector.

It listed on the HKEx in 1993 and the SSE in 1994. In 1993, Maanshan Steel was spun off from state-owned Maanshan Iron Mining Plant, founded in 1953, which was split into Maanshan Steel and Magang Group Holding Company Limited (Masteel). Maanshan Steel's principal activities are producing and selling iron and steel products. The company imports raw ore and machinery. Maanshan Steel's primarily ore supplier is Maanshan Steel's sister company, Masteel.

Maanshan had a market capitalization of US\$3.02 billion in April 2012.¹⁰² Internationally, Maanshan Steel had US\$254.76 million in combined revenue in 2011, which included revenue in Hong Kong. The company disclosed an international tax bill of US\$0.45 million in Hong Kong and US\$11.32 million in countries outside of Hong Kong and mainland China in 2011.

PetroChina

Key findings:

- Disclosure of aggregated overseas income taxes and taxes other than income taxes
- Disclosure of domestic payments for exploration and mining rights
- Participation in EITI
- Expression of support for some provisions outlined by US Dodd-Frank legislation

PetroChina Company Limited (PetroChina) is the publicly traded arm of the state-owned China National Petroleum Corporation (CNPC), which grew out of the Chinese Fuel Industry Ministry, founded in 1949. PetroChina was established in 1999 as part of a restructuring of CNPC, and is primarily involved in extracting, refining and selling petroleum, natural gas and related products.

Listed on the NYSE (NYSE: PTR) and the HKEx (SEHK: 0857) in 2000 and on the SSE (SSE: 601857) in 2007 (energy sector), PetroChina was the third largest company in the world by market capitalization with a market value of US\$294.73 billion in April 2012.¹⁰³ With US\$21.13 billion in net profit in 2011, PetroChina was the second most profitable company in China and the eleventh most profitable in the world.¹⁰⁴ Internationally, PetroChina had US\$91.43 billion in overseas revenue in 2011.

The company reported US\$1.82 billion in international income tax paid and US\$3.02 billion in other international taxes in 2011. PetroChina's international property acquisitions and exploration costs totalled US\$576 million; and their international development costs were US\$1.71 billion in the same year. However, PetroChina only reported a domestic expense of US\$129.13 million on exploration and mining licenses, also in 2011.

Among the 17 countries where PetroChina reported overseas operations in 2011, the company was active in three EITI compliant countries (Peru, Niger and Azerbaijan) and four EITI candidate countries (Chad, Iraq, Indonesia and Kazakhstan).¹⁰⁵ According to the Mongolia EITI Reconciliation Report 2011, PetroChina dachin tamsag LLC – the company's joint venture in the country – contributed 3.0% of the total payments to governmental organizations covered by EITI.¹⁰⁶ PetroChina's parent company CNPC has disclosed revenue information for several of Mauritania's EITI reports.¹⁰⁷ CNPC was elected to Iraq's EITI council in 2011 – the first time a Chinese company had been elected as an EITI country representative.¹⁰⁸

PetroChina publicly showed its support for some provisions of the Cardin-Lugar Amendment (Dodd-Frank 1504) in the US in its letter to the Securities and Exchange Commission (SEC) and indicated its willingness to report on payments on a country-by-country basis.¹⁰⁹

Shanxi Coal International

Key findings:

- Disclosure on total overseas revenue

Shanxi Coal International Energy Group Company Limited (Shanxi Coal International) is primarily engaged in coal mining and trading, and railway transportation. The company was solely incorporated by Shanxi Coal Import & Export Group Company Limited and it was listed on the SSE (SSE: 600546) in the industrials sector (CSRC Extractive Industry category) in 2009. The market capitalization was US\$2.76 billion in December 2012.¹¹⁰

Shanxi Coal International mines and processes coal from China for domestic and international sale, and the company's foreign clients are in over 20 countries and territories. The company's overseas revenue increased three-fold from US\$24.36 million in 2010 to US\$69.58 million in 2011.

Shenhua Energy

Key findings:

- Disclosure on domestic exploration license fee and coal selection and mining fees
- Disclosure of total amount of overseas revenue

China Shenhua Energy Company Limited (Shenhua Energy) is the public subsidiary of the key Chinese state-owned enterprise Shenhua Group Corporation Limited (Shenhua Group). Established in 2005, Shenhua Energy is the largest coal producer in China and also owns power, rail and port operations in the country.¹¹¹ With pre-tax profit in 2011 of US\$10.59 billion and market capitalization of US\$84.2 billion, Shenhua Energy was the seventh largest company in China by both profit and market value.¹¹² Shenhua Energy was listed on the HKEx (SEHK: 1088) and SSE (SSE: 601088) energy sector (extractive company by CSRC's classification) in 2005 and 2007, respectively.

Shenhua Energy did not report its SCVPS in 2011, but reported a contribution of US\$0.67 per share in 2010. Shenhua Energy in 2010 reported Coal Selection and Mining Fees of US\$781.8 million as cost of revenue for IFRS, and exploration license fee of US\$453.8 million for CAS; in 2011, the coal selection and mining fees were US\$1.03 billion and the exploration license fee was zero.

Internationally, the company has a mining operation "Watermark Coal Project" in Australia and a coal fed power plant in South Sumatra, Indonesia. Shenhua Energy is currently in discussion for a major stake in the large Mongolian mine, Tavan Tolgoi.¹¹³ Indonesia is an EITI candidate country and Mongolia is an EITI compliant country; as a result, the countries will have to publish the cost of work plans for all separated extractive projects, including Shenhua Energy's projects. The company reported it paid 30% and 25% of income tax respectively to Australia and Indonesia in 2010 and 2011. However, only the total amount of overseas revenue was made available (US\$923.5 million in 2010, US\$557.2 million in 2011).

Sinopec

Key Findings:

- Published two production licenses in Angola
- Paying 50% rate of income from Angola block to host government
- Participated in Gabon EITI Report 2006
- Included in disclosure the total domestic exploration license fees and production right usage fees
- Provided supplemental information on oil and gas exploration and producing activities in US '20-F' disclosures

China Petroleum & Chemical Corporation (Sinopec) is the largest producer and supplier of refined oil products and major petrochemical products in China, and also the country's second largest oil and gas producer.¹¹⁴ The company's business primarily includes exploration, development, production and trading of petroleum and natural gas; and refining, marketing and distribution of petroleum products and chemicals.

Sinopec was incorporated in 2000 by the state-owned China Petrochemical Corporation and the company was listed on the HKEx (SEHK: 0386), NYSE (NYSE: SNP), LSE (LSE: SNP), in the same year. In 2001, the company was listed on the SSE (SSE: 600028) in the energy sector (CSRC's extractive industry category). The market value of Sinopec was US\$104.2 billion in April 2012.

Sinopec first acquired foreign oil in 2010 when it paid US\$2.5 billion to buy a stake in an Angolan oil field.¹¹⁵ The company currently holds two production licenses in the Angola Block 18, paying a 50% rate of income to the Angolan government.

Sinopec disclosed its total exploration license fees and production right usage fees payments (2010: US\$71.65 million; 2011: US\$69.74 million) to the Ministry of Land and Resources of China.¹¹⁶ In accordance with the *Extractive Activities – Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures* provision issued by the Financial Accounting Standards Board (FASB) of the United States, the company provided supplemental information on oil and gas exploration and producing activities. For the year 2011, Sinopec's aggregated income tax for oil and gas producing activities was US\$3.52 million; taxes other than income tax US\$6.94 million.

Response to SynTao -Global Witness findings

Sinopec stressed that it strictly follows the disclosure requirements of the stock exchanges it is listed on – Shanghai, Hong Kong, New York and London.

Sinopec said that it was aware of the US SEC's new disclosure rules for extractive companies and that it was preparing to report its payments to overseas governments for the annual report for the 2012 financial year.

The company confirmed the findings in this report and, specifically, that it has an operational site in Angola (Block 18). The company also noted that it does not have upstream assets in Gabon and Azerbaijan. Therefore, information in Gabon's and Azerbaijan's EITI reports may refer to Sinopec's parent company, China Petrochemical Corporation (Sinopec Group).

Wuhan Iron and Steel

Key findings:

- No overseas information disclosed except that it has subsidiaries in Singapore and Indonesia

Wuhan Iron and Steel Company Limited (Wuhan Iron and Steel), a wholly owned listed subsidiary of state-owned Wuhan Iron and Steel (Group) Corporation (WISCO), is a company engaged in the manufacture and distribution of iron and steel products. As of December 31, 2010, the Company had three subsidiaries and three affiliates, which involved in the manufacture and distribution of oxygen, metal products, coke and coal.¹¹⁷

Wuhan Iron and Steel was listed on the SSE (SSE: 600005) in 1999. The SSE categorizes the company in the Material Sector Index. The CSRC qualifies Wuhan Iron and Steel as part of the manufacturing-metal industry. Wuhan Iron and Steel's market capitalization was US\$4.85 billion in April 2012.¹¹⁸ SCVPS of the company was US\$0.16 in 2011.

Wuhan Iron and Steel distributes its products primarily in domestic markets, although in its 2011 corporate communications, the company disclosed the profiles of its subsidiaries in Singapore and Indonesia, whose main business is trading and investing. The company did not disclose the payments they made to host governments.

Yanzhou Coal

Key findings:

- Disclosure of domestic fees for mining rights
- Detailed disclosure of income tax rate in Australia
- Disclosure of total revenue in various countries

Yanzhou Coal Mining Company Limited (Yanzhou Coal) is an integrated coal enterprise that was founded in 1973. Its parent company is Yankuang Group Corporation Limited, the fourth largest state-owned Chinese coal mining enterprise. In 1998, Yanzhou listed on the HKEx (SEHK: 1171), SSE (SSE: 600188) industrials sector (CSRC's extractive industry classification) and NYSE (NYSE: YZC). It is the only Chinese coal company to be listed on three exchanges.

In 2011, Yanzhou Coal had pre-tax profits of US\$1.99 billion and had a SCVPS of US\$0.8, the highest of any companies compared in this report. The company had a market capitalisation of US\$16.1 billion, as of April 2012.¹¹⁹ Yanzhou Coal disclosed on IFRS US\$135.18 million fees for mining rights in 2011.

Along with its operations in China, Yanzhou Coal mines potash in Canada and coal in Australia. The company only separately reported on the US\$40.6 million of revenue it gained in Australia in 2011. Yanzhou Coal reported that for Australia it paid 30% income tax on its revenue, 10% goods and services tax, 4.75-9% fringe benefits tax and 7-8.2% resource tax. In addition to revenues from operations in Australia, Yanzhou earned total revenue of US\$1.35 billion in other countries including South Korea, Japan, Canada and Luxembourg in 2011. Yanzhou did not report on its taxes and other payments to other foreign governments.

Response to SynTao -Global Witness findings

Yanzhou Coal stated that its disclosure strictly follows the rules set by the SSE.

The company said that it disclosed the domestic fees paid for mining rights because they were part of an (unspecified) asset acquisition according to the *Content and Format Rules for Information Disclosure by Companies Offering Securities to the Public No. 2 -- Contents and Format of Annual Reports*.

The company explained that they must disclose the main taxes paid to the Australian government

in its corporate communications because Yancoal Australia is a holding subsidiary of Yanzhou Coal in Australia. Yancoal's revenue was a major part (20.6%) of Yanzhou Coal's total revenue over financial year 2011. As a result the company needed to disclose Yancoal's payments to provide full insights into its "geographical information of sales".

Zijin Mining

Key findings:

- Overseas project profiles are available on the company's English website, but not on the Chinese website
- Disclosure of the amount of tax payment to Tajikistan
- Disclosure of income tax paid to Hong Kong

Zijin Mining Group Company Limited (Zijin Mining), based in Fujian Province, is the biggest gold producer and second biggest copper producer in terms of volume in China. The company's business also covers other metals such as silver, molybdenum, lead and zinc.

The predecessor of Zijin Mining was the wholly state-owned company Shanghang County Mineral Company. A group of eight companies, led by MinxiXinghang State-owned Assets Investment Company Limited, established Zijin Mining Group Company Limited in 2000 as a joint stock limited company.

Zijin Mining was first listed on the HKEx (SEHK: 2899) in 2003, and was listed in the material sector (CSRC's extractive industry) of the SSE (SSE: 601899) in 2008. The market capitalization of the company was US\$13.4 billion in April 2012. By the end of 2011, the company's total assets were US\$8.33 billion, an increase of a third on the figure for 2010.

Zijin Mining and its subsidiaries own 43 overseas exploration rights and 6 overseas mining rights. On its English website, profiles are available for overseas projects in Australia (Norton Gold Fields Paddington Gold Mine), Democratic Republic of Congo (Misisi Gold Project and Mpotoko Gold Project), Mongolia (NalinTolgoi Gold Mine), Mozambique (Manica Gold Project), Myanmar (Moweitang Nickel Project), Peru (Whiteriver Copper-Molybdenum Mine), Russia (Tuwa Zinc Mine) and Tajikistan (ZGC TarorGold Mine).

Zijin Mining is the only company covered in this study that reported on its payment to a single country, outside of Hong Kong and Taiwan. It disclosed that it paid

Table 6 : Level of disclosure of overseas government payments made by companies, 2010 and 2011

Company listed on SSE	Level of detail reported	Total overseas revenue	Revenue at country level	Total overseas tax paid	Proportion of overseas tax at country level	Total overseas tax at country level
Aluminum Corporation of China		x			x	
Baoshan Iron and Steel		x				
Baotou Steel						
China Coal Energy		x			x	
China Oilfield Services		x		x	x	
Gan Su Jiu Iron and Steel						
Jiangxi Copper		x	x		x	x (i)
Maanshan Iron & Steel		x		x		x (ii)
PetroChina		x		x	x (iii)	
Shanxi Coal International		x				
Shenhua Energy		x			x	
Sinopec				x	x	
Wuhan Iron and Steel						
Yanzhou Coal Mining		x	x		x	
Zijin Mining						x (iv)

i. Income tax was published for Hong Kong

ii. Tax bill was published for Hong Kong

iii. Data published within EITI report

iv. Taxes and fees paid to Tajikistan and Hong Kong published

US\$18 million in taxes and fees to Tajikistan in 2011.¹²⁰ The company has established a close relationship with the Tajikistan government as the ZGC Gold Mine is the largest gold producer in the country. Zijin Mining also disclosed that it paid US\$484 in income tax to the Hong Kong government in 2011.

Summary

Chinese companies tend to disclose on items that are required by domestic regulation and guidelines. Few companies provide extra information, especially on overseas operations. Among the 15 companies covered in this study, six companies reported (limited) information about overseas tax payments and ten companies disclosed some information linked to overseas revenues, such as aggregated or country specific revenue gained overseas, total amount or percentage of income tax paid to host government. In general, these amounts were disclosed without providing a breakdown on country specific information.

Overall, the three oil companies, Sinopec, PetroChina and China Oilfield Services, offer more information to stakeholders and are more willing to adopt international reporting standards. Zijin Mining proved to be an exception, as it reported on its tax payments to Tajikistan, which shows that Chinese companies seem to have the capacity to adopt international best practice and report on specific payments to (host) governments when they choose to.

Social contribution value per share (SCVPS) is an innovative attempt to give stakeholders an indication of companies' impact on society. However, the values are not comparable between companies and it is not clear how items included in the formula are calculated. This research suggests that the SCVPS would be more useful if improvements were made to how it is calculated.

5. Stakeholder Engagement

Chinese and international stakeholders from the extractive, investment, non-governmental (NGO) and academic communities answered a five question survey for this report. Some 24 respondents gave their perspectives on:

- the benefits and disadvantages of increased extractive industry government payment disclosure;
- the feasibility and pros and cons of the Shanghai Stock Exchange (SSE) expanding extractive industry payment reporting requirements;
- the effectiveness of the SSE's transfer of mining rights disclosure and social contribution value per share (SCVPS) systems;
- and Chinese involvement in the Extractive Industries Transparency Initiative (EITI).

The results of the survey add value to the discussion on expanding reporting of extractive industry payments to governments because until this point, there has been little focus on the Chinese extractive industry. The respondents provided in-depth perspectives and analysis of many of the most salient issues in the debate over expanding government payment reporting, especially in China. The focus of this study was on the perspective of Chinese stakeholders, which had been missing in this debate.

By the end of May 2012, 98 email requests to participate in this survey had been sent out; 49 went to international stakeholders and 49 requests went to Chinese stakeholders. Requests were followed up by explanatory phone calls, emails and meetings. There was a 22% overall response rate to survey requests, including 15 replies from international stakeholders (30% response rate) and 7 replies from Chinese stakeholders (14% response rate). Stakeholder responses varied greatly in length and detail. Typically, responses from Chinese participants were more direct and their explanations for their answers were shorter when compared to responses from foreign respondents.

Question 1: What benefits, if any, do you see regarding the disclosure of payments made by Chinese extractive companies to governments overseas?

All respondents answered this question.

Key Findings

- A significant portion of Chinese and foreign respondents, 8 of 22, pointed out that increased payment reporting would improve the global reputation of Chinese extractive companies.
- Nearly half of all respondents, 10 of 22, stated that investors would benefit from greater payment transparency because they would be better able to analyse company risks.
- A large majority of Chinese respondents, 6 of 7, said that increased payment reporting would improve corporate and government transparency.

Importance of company reputation to investors

Chinese and international respondents expressed a great awareness that increased disclosure practices offer Chinese companies a chance to shake off unwanted association with corruption and unethical conduct. Respondents felt that increased disclosure practices would help Chinese companies build more credible corporate reputations. Increased transparency was not only considered intrinsically important, but it would also help attract investors. As one international sustainable development and education organisation active in China noted:

Increased reporting will “benefit investors when comparing the payment differences between different countries to make their investment decision. It can also help extractive companies create a more creditable image.”

It was felt by several respondents that increased credibility and investor interest will help Chinese extractive companies gain access to investors from more developed markets, which will help these companies diversify their investor base.

Mitigating investor and company risk

Chinese and international respondents from both the private and public sectors recognised that reducing risk was a major benefit of increased extractive industry reporting. Respondents generally felt that by requiring Chinese extractive companies to provide clear government payment information, the SSE would protect investors by reducing risk.

Respondents also noted that increased payment reporting would improve communications between companies and investors, which would both help investors understand the different risks companies face, and help companies better understand their investors' concerns. For example, two respondents felt that greater payment reporting would increase investors' understanding of the political risks extractive companies may face in different countries. This reasoning is in line with more than 80 institutional investors and 70 global extractive companies that have publicly expressed their support for the Extractive Industry Transparency Initiative.¹²¹

The following quote from a major international asset manager (Kwai San Wong, Governance and Sustainable Investment analyst, F&C Investments) expressed respondents' general sentiments about the virtues of expanded payment transparency.

"[Clear payment information] may enable better clarity about individual companies' exposure to country-specific risk, by shedding light on the degree of political risk the company is exposed to, particularly in the event of a change in government."

Chinese focus on transparency

Many international survey respondents spoke of transparency in the context of reducing investor risk and improving company reputations. By contrast, Chinese respondents overwhelmingly brought up increased transparency as one of the signature virtues of increased extractive industry government payment reporting. This view is consistent with growing attention in China about the importance of transparency for both state-owned enterprises (SOEs) and private companies.¹²² Responses to this survey solidified that increasing corporate transparency is highly important to many Chinese stakeholders, both private and public.

Grey area between SOE actions and government policy

We note that two foreign respondents discussed the vague distinction between international aid contributions from the Chinese government, and payments from Chinese state-owned enterprises (SOEs) to foreign governments for access

to extractive resources. One respondent (Hans-Ulrich Beck, Global Director, Research Products, Sustainalytics) pointed out that payments to host governments by Chinese extractive companies should be seen within a broader context of aid and economic benefits the Chinese government offers to host governments in return for projects and licenses granted to its companies. Therefore, financial payments from a Chinese SOE may not necessarily reflect the total private payments, investments or transfers made to a host government. Instead, the extractive company's payments may be part of a larger strategic deal between governments.

While Chinese extractive companies' activities cannot always be viewed in isolation of Chinese government policy, respondents still felt that increasing transparency of payments to foreign governments will provide essential information to investors. Moreover, stakeholders argue that increased extractive industry payment transparency would complement a recent push for increasing overall transparency in China.

Question 2. What disadvantages, if any, do you see regarding the disclosure of payments made by Chinese extractive companies to governments overseas?

All respondents answered this question.

Key Findings

- The most common concern was that expanded government payment reporting would reduce the competitiveness of Chinese companies, mentioned by 7 of 22 respondents.
- Asset managers and NGOs from both China and abroad, 4 of 22, directly stated that there are *no disadvantages* to the SSE expanding reporting requirements.
- Some Chinese respondents have articulated that Chinese culture may not be comfortable with the principle of transparency and consider disclosing financial information to be a disadvantage.
- Companies may face increased scrutiny from citizens, NGOs and watchdog groups once these stakeholders have increased disclosure of financial information.

Concern about an unequal playing field

Some respondents held that internationally active resource extraction companies which are subject to increased transparency requirements may be put at a disadvantage when bidding for projects against companies not subject to

transparency regulations. This is a common concern, but in contrast, two international respondents from the finance sector (Kwai San Wong, Governance and Sustainable Investment analyst, F&C Investments) disputed its logic.

They stated that as more countries participate in EITI and

“...with the passage of Section 1504 of the Dodd Frank Act in the US, all major western operators are already subject to such [reporting] standards. This would severely restrict the universe of potential suppliers, thereby both lowering competition and quality and raising costs and operating risks for host governments.” (F&C Investments)

Increased expectations

A few respondents warned that increased financial disclosure would lead to increased public awareness about the revenues gained in exchange for exploration rights and transfer of mining rights, which may heighten expectations for Chinese extractive companies to address economic and social hardships in host countries. Similar to many international extractive companies, state-owned Chinese companies may not be comfortable to interfere with a host countries' internal politics. One Chinese organisation (Karl McAlinden, Project Manager, Institute of Public & Environmental Affairs, IPE) focused on overall trade relations, stating that increased reporting regulations may lead to the “deterrence of Chinese companies in investing overseas, which could negatively affect bilateral trade.”

Poor payment comparability and traceability

A respondent (an international investment research provider) argued that it may remain difficult to analyse the payments of one company compared to those of another company. This is because extractive industry and government payment reports, such as some EITI reports, often lack contextual information about local laws, regulations, project contracts, and the precise distribution of funds. They argue that consequently, analysts will have trouble distinguishing if extractive industry payments are channelled into government funds that are used for “legitimate” purposes, or if payments are used for state-sponsored projects that are not in the interests of citizens. Such difficulty in comparing different companies' payments would be an impediment for investors and other stakeholders, such as industry watchdog groups, when analysing a company's payment information.

Concern about increased operational costs

Only one respondent, an international asset manager (Kwai San Wong, Governance and Sustainable Investment analyst, F&C Investments), brought up the concern that Chinese companies would face increased operational costs from having to report country-level government payment

information. Extractive companies often make this claim¹²³, so it is interesting that only one respondent to this survey mentioned it. Nevertheless, the respondent minimized any concern over increased operational costs, stating:

“Companies will incur higher costs, but the increased reporting requirement will bring about more stability and balanced economic development. This will mean lower investment risk and a potential for enhanced wealth creation.” (F&C Investments)

Question 3. To what degree is it feasible for the Shanghai Stock Exchange to:

- a) synchronize its regulations with the Hong Kong Stock Exchange (HKEx) in requiring extractive companies to disclose payments made overseas at the point of listing and, moreover,
- b) introduce annual disclosure requirements as likely will happen in the United States and the European Union?¹²⁴

Of all respondents, 13 out of 15 foreign interviewees and 5 out of 7 Chinese interviewees answered this question.

Key Findings

- Nearly half of international respondents, 7 of 15, explicitly supported the SSE synchronizing its regulations with the HKEx, or pending requirements in the US or EU.
- Zero international respondents were explicitly against the SSE enacting these requirements.
- A majority of Chinese respondents, 4 of 7, questioned the feasibility of the SSE synchronizing its extractive industry reporting requirements with the HKEx or other international disclosure requirements.
- In contrast, an important proportion of international respondents, 5 of 15, stated that it was technically feasible for the SSE to synchronize its reporting requirements with HKEx, US and/or European requirements.
- Half of Chinese respondents questioned the reliability of the government payment information published by both host governments and extractive companies.

Broad support from international respondents

Both private and non-profit international investors warmly welcomed the prospect of the SSE requiring extractive companies to report their payments at a

country level at the time of initial public offerings (IPOs), similar to HKEx requirements, or annually, similar to US and EU requirements. Many organizations felt that having disclosure requirements similar to other exchanges would help create an “*even playing field*” for investors when they are considering extractive investments by making it easier to compare the financial positions of companies’ activities in different countries.

Feasibility questions

Chinese respondents were cautious about the feasibility of the SSE bringing their reporting requirements into line with either the HKEx’s requirements or international standards. One Chinese industry trade group (Liang Xiaohui, Chief Researcher, Office for Social Responsibility, China National Textile and Apparel Council (CNTAC)) stated: “*The feasibility is not high in the near future – unless the SSE applies a regulation on all listed companies (or a transparent governance index).*”

Chinese concerns over feasibility stood in contrast to statements from many foreign respondents that it would be technically feasible for the SSE to require expanded payment reporting at the time of listing or annually. Additionally, international respondents also felt that Chinese extractive companies would be capable of providing the information.

The discrepancy between Chinese and international respondents’ feelings was likely due, in part, to international respondents focusing on the technical feasibility of synchronization, or the idea that companies have the capacity to report payments. Chinese respondents instead focused on the difficult political feasibility of the SSE synchronizing its reporting requirements with other exchanges. In terms of concern about the political feasibility of synchronization, international respondents generally echoed the concerns of Chinese respondents.

Questioning veracity

Chinese stakeholders also questioned the veracity of country-level payment information. These concerns echo recent comments by Chinese investors¹²⁵ about suspect accounting practices of some listed Chinese companies. Specifically, investors are concerned about the accounting practices of large extractive companies, and singled out Sinopec and CNPC, the parent company of PetroChina. To remedy questions about the accuracy of reported payments to governments, some survey respondents suggested that the SSE should require third-party verification of payment information.

Industry interest

Interestingly, one Chinese extractive company was not completely dismissive about the feasibility of introducing

payment reporting requirements. The company stated that the feasibility of synchronizing SSE reporting requirements with HKEx or international requirements “*depends on the government’s requirement on making SOE related information fully available to the public.*”

The company was clearly concerned with SOEs having to make financial information wholly open to the public, but it was not completely dismissive of synchronizing SSE reporting standards with international standards.

Question 4. What are the pros and cons of the existing Shanghai Stock Exchange regulations on

a) obtaining and transferring of mining rights and

b) Social Contribution Value Per Share (SCVPS)? Does the disclosure of right and social contribution information contribute to “win-win”¹²⁶ development in countries overseas in line with the policies of the Chinese government?

Of all respondents, 10 out of 15 foreign interviewees and 4 out of 7 Chinese interviewees answered this question.

Key Findings

- Less than one-third of respondents, 4 of 14, felt that the current information on mining rights and SCVPS was useful.
- More than one-third of respondents, 5 of 14, stated that if companies provided consistent and transparent reporting of SCVPS, then the formula would be a useful indicator for investors.
- Respondents are concerned that investment products, such as investment indices, are based on SSE’s SCVPS even though there is no publicly-announced verification of SCVPS.
- SSEs initiatives, disclosing mining rights and SCVPS, are insufficient to foster “win-win” development as they lack focus on the impact of overseas operations.
- No respondents commented on the SSE instruction regarding the obtaining and transfer of mineral rights.

SCVPS, a progressive concept but flawed in execution

Respondents focused on SCVPS and commented little on the SSE’s reporting requirements on obtaining and transferring mining rights (refer for the calculation of SCVPS on p. 18). They commended the SSE for enacting SCVPS and viewed the principle of SCVPS, capturing

corporate contribution to society, as a meaningful idea and a “*unique Chinese characteristic*” (Dr Xinting Jia, Principal, Mercer). At the same time, the majority of survey respondents also felt that SCVPS is difficult for external parties to comprehend and respondent opinion was divided about the real analytic value of the metric.

Respondents felt that the data required to calculate SCVPS leave too much room for interpretation because there is no clear definition for the parameters to be used. The payments that should be included in each item are not always clear. For instance, in the case of donations, it is not clear whether private employee donations are included. Also, guidance seems to be lacking on how the last item of the formula “*other value for shareholders*” should be calculated.

Respondents also felt that SCVPS data can “*mislead*” investors because companies present a limited breakdown of the SCVPS scores in their annual reports. SCVPS reporting does not require disaggregation and quantification of the benefits to local communities at home or abroad. This led respondents to feel that the score provides little insight to a company’s investors and other stakeholders about how the company is actually contributing to society. The overall lack of transparency and reporting requirements makes evaluating SCVPS scores difficult for investors.

A Chinese industry trade group (Liang Xiaohui, Chief Researcher, Office for Social Responsibility, China National Textile and Apparel Council (CNTAC)) summarized the conflicted view that many Chinese and international respondents had about SCVPS:

The SCVPS calculation still needs to include damage caused by both direct environmental impact and from illegal activities, such as corruption and product quality crisis. It [SCVPS] seems to make a positive contribution, but it does not completely show the social influence of many companies. Of course the SSE should be encouraged for exploring social disclosure. In the future, we expect that the method for calculating SCVPS calculation will gradually improve.

A few respondents noted that SCVPS’ impact was limited not only by its ambiguous formula and requirements for calculating the SCVPS score, but also due to its voluntary nature. Since SCVPS is voluntary, some companies may only report it when they feel the score is complimentary. For example, it is unclear why Shenhua Energy Group reported their SCVPS in 2010 but did not report it in 2011. The company did not release a statement explaining their decision.

Respondents expressed a desire for the SSE to clarify SCVPS because “*SCVPS is one of the most important indicators when doing SRI (socially responsible investment) assessment*” (as one sustainable fund manager in China mentioned) for

investment products. For example, the China Construction Bank SSE Social Responsibility Index Exchange Traded Funds (CCB SSE Social responsibility Index ETF), is based on the top 100 ranked companies according to their SCVPS.

Win-win development?

Both Chinese and international respondents argued that the current effects of mining rights transfer disclosure and SCVPS is limited in creating win-win development in overseas countries. An important reason for this limited effect is that most Chinese companies see social contributions to society as charity projects such as building schools, hospitals and roads in host countries. However, as one NGO representative (Adina Matisoff, Researcher, Friends of the Earth-US) noted, SCVPS and mining rights transfer reporting are “*insufficient to foster ‘win-win’ development for the communities and ecosystems that are directly impacted by extractive industry projects*” because they need to have a greater focus on the environmental and social impacts extractive companies have in host countries.

Mineral right disclosure

No respondents mentioned the SSE instruction on the obtaining and transfer of mineral rights. This mirrors the lack of reference to the instruction in the annual reports. Similar to the SCVPS, the measure is an innovative way of promoting transparent management of resources. However, it appears that it is not currently valued by stakeholders in the sector or implemented.

Question 5. Are you aware of information Chinese extractive companies are currently producing through the Extractive Industry Transparency Initiative (EITI) and how do you perceive the participation of companies in the scheme?

Of all respondents, 12 out of 15 foreign interviewees and 5 out of 7 Chinese interviewees answered this question.

Key Findings

- Majority of respondents, 11 of 17, are aware that Chinese resource extractive companies are producing information through EITI.
- Half of Chinese respondents stated that Chinese extractive companies will need to be involved with EITI if they want to be global players.
- International stakeholders identify Chinese companies to have reported under the EITI framework in the following countries: Iraq, Gabon, Kazakhstan, Mongolia and Nigeria.

Respecting EITI and local regulations

A majority of respondents were aware that Chinese resource extractive companies respect local laws and regulations in EITI-Compliant and EITI-Candidate countries by reporting in conformity with EITI and government requirements. However, EITI reporting and involvement from Chinese extractive countries rarely go beyond compliance. As one global asset manager (Kwai San Wong, Governance and Sustainable Investment analyst, F&C Investments) put it:

“Chinese companies report strictly in countries where this is a legal or regulatory requirement, but refrain from making this the subject of a group wide corporate policy commitment to transparency in the way that EITI-signatory extractive companies have done.”

Respondents also noted that while Chinese extractive companies report their payments in individual country EITI reports, they do not publicize the information they report or publish it in any other arena. Generally, respondents showed a clear desire for Chinese extractive companies to step-up their involvement in EITI and join other global extractive companies (such as RioTinto and Statoil) in encouraging government and corporate transparency.

Chinese participation

According to Chinese respondents, the participation of Chinese companies in EITI is important and needs encouragement because it is a vital step in strengthening Chinese foreign relations. An academic respondent from China (Professor Guo Yi, Beijing Technology and Business University (BTBU)) noted that:

“Participation in EITI is an important way to establish credibility within the extractive industry. It provides evidence that [Chinese] overseas investment and cross-cultural management are in accordance with the regulation.”

However, Chinese respondents also expressed concern over the quality of information disclosed in EITI reports, in terms of completeness and accuracy, and were cautious about trusting the veracity of report data. These respondents felt that information in some host country EITI reports may not be accurate and worried that legal and reputational problems may arise for Chinese extractive companies because there is no external legal framework for enforcing EITI. One Chinese respondent stated that disadvantages may overcome advantages for Chinese companies to participate in the framework.

Some of the respondents who are concerned with enforcing EITI regulations do not take into account that the EITI

regulates and monitors country reports and will revoke a country’s status of an EITI Candidate or Compliant Country if it does not abide by EITI regulations. Madagascar, for example, had its EITI Candidate Country status suspended because EITI did “*not believe that the relationships necessary for effective EITI implementation in Madagascar [were] currently possible and capable of being sustained.*”¹²⁷

CNPC in Iraq

Several respondents mentioned CNPC’s disclosure on operations in Iraq because this was an example where a Chinese extractive company has gone beyond compliance to take a leadership role in a country’s EITI process. A major European institutional investor and pension fund service provider (Saskia van den Dool-Gietman, Senior Advisor Responsible Investment, PGGM Investments) values increased Chinese EITI involvement (such as CNPC’s activities in Iraq) and encourages Chinese extractive companies to “*formalize their support*” for EITI.

Summary

Addressing risk, whether to companies or investors, was a common theme in answers from both Chinese and international respondents. International respondents felt that if the SSE increased government reporting requirements for Chinese extractive industries, risk would decrease for all parties involved. Such reduced risk would: foster a more stable business environment in host countries for Chinese extractive companies; provide more reliable information and returns for investors; and increase the likelihood that residents in host countries would see financial and development benefits from extraction of their natural resources. Chinese respondents mentioned these benefits too, but focused more on improving transparency and the veracity of payment information from Chinese extractive companies and host countries.

Respondents from China and abroad held Chinese and SSE efforts to improve transparency and corporate social responsibility in high regard. Many respondents referred to these initiatives as being unique and promising, but the same respondents also felt that officials in the SSE and Chinese government needed to enforce and clarify these regulations. These measures lack legitimacy in the eyes of both Chinese and international stakeholders because enforcement is inconsistent and unclear.

With Chinese and international stakeholders from the investment, private and public sectors clearly siding with the overall benefits of increased reporting of extractive industry payments to governments, it is in the SSE’s interest to seriously consider the many benefits which would come from enacting such regulations.

6. Conclusion

The Shanghai Stock Exchange plays an important role within China in promoting improved corporate disclosure and has already taken encouraging actions to improve social responsibility reporting of listed companies. However, our research shows that current financial disclosure by the largest SSE-listed extractive companies is scattered and limited. Compared to the other international initiatives, the SSE is still far behind the global trend of increasing overseas payment transparency.

Research results show that promoting transparency is significant for Chinese extractive industry stakeholders. Investors are keen to mitigate corporate risks and, as such, are interested to learn more about increasing transparency of extractive industry payments to host governments.

Within the context of rising global concern about transparency in the resource extractive industry, this report recommends that the SSE adopt international best practice standards similar to the HKEx, US Dodd-Frank 1504 and EU's Transparency Directive. It should make amendments to its transparency and accounting

directives to mandate listed oil, gas and mining companies to annually disclose payments to overseas governments on a country by country and project by project basis in publicly accessible reports.

Enhanced disclosure on payments made to host governments would allow investors and the public to better assess and understand the financial risks associated with resource extraction companies and the value that these companies create for China as a whole. Furthermore such measures coincide with the SSE's aim to make companies demonstrate their 'social contribution' to a harmonious society.

The SSE operates on the principle of "legislation, supervision, self-regulation and standardization" with the aim of creating an "open, safe and efficient marketplace".¹²⁸ The SSE has a great opportunity to improve standardization, transparency and to leverage its leadership by requiring disclosure on payments to overseas governments. By doing so, Chinese companies will better realize "win-win" relationships with foreign governments, populations and corporations alike.

7. Recommendations for the SSE to increase transparency in the oil, mining and gas industries

On the basis of the findings in this study, we suggest that the Shanghai Stock Exchange (SSE) reviews its existing sustainability disclosure requirements, especially targeted at the resource extractive industry. Ample scope exists for improving guidance on financial disclosure, including the definitions of information to be published, such as the Social Contribution Value Per Share.

We recommend that the Shanghai Stock Exchange considers mandating resource extractive companies to annually report on payments to governments on a country and project level, including payments made to the Chinese government.

The results of the company assessments and stakeholder survey in this report show that a considerable number of Chinese companies listed on the SSE already hold the capacity to report detailed payments on domestic and overseas projects and that stakeholders would welcome increased transparency requirements for oil, gas and mining companies. By introducing payment disclosure rules for the resource extractive industries, the SSE can:

- Reclaim its sustainable leadership among stock exchanges that the SSE gained when it first implemented Social Contribution Value Per Share (SCVPS) in 2008;
- Give investors access to more relevant data needed to assess the risks companies face in an inherently uncertain industry;
- Free companies from potential conflicts with resource-rich governments;
- Encourage better stewardship of resource revenues and hence a more stable and less risky environment; and

- Help reduce conflict and citizen mistrust in areas of Chinese company operation through building a social license to operate.

Key arguments and suggestions for action

Leverage SSE's Leadership

The SSE could review its existing requirements and update its sustainability disclosure guidelines, especially targeted at the resource extractive industry

The SSE defined itself in 2008 as a sustainability leader when it launched two notices encouraging listed companies to release information about their sustainability performance. Notably, the stock exchange introduced a method to measure companies' value creation for society, a formula called Social Contribution Value Per Share (SCVPS).¹²⁹ In 2008, the SSE also authorized a specific article aimed at the resource extractive industry that requires companies to detail mineral rights acquisitions and transfers in their annual reports.¹³⁰

SSE's leadership position has diminished in recent years because other exchanges have enacted more stringent requirements, such as promoting sustainability awareness and reporting standards for IPOs or as ongoing listing requirements.¹³¹ The SSE can reclaim its principal position by introducing requirements for the extractive industry to disclose payments to governments on a country-by-country and project-by-project level.

From the company and stakeholder studies in this report, it is clear that:

- the SSE's conditions on disclosure do not always increase clarity and guidance;
- company reporting on payments is irregular and fragmented;

- the SSE is deficient in requiring mandatory third party verification;
- and many stakeholders feel uncertain about how to work out a standardized SCVPS score.

The SSE boasts a high number of listings operating in, or closely connected to, the resource extractive industries. All extractive companies on the SSE generating considerable revenue can be expected to make large payments to (host) governments. However, the SSE has not formulated special disclosure requirements for the extractive companies.

Minimize Investor Concerns Over Extractive Industry Risk

Imposing reporting requirements on extraction companies listed on the SSE provides investors with a platform to better assess extractive companies' project portfolio and risk exposure

If investors receive access to more material information that may affect their investment decisions, it will become easier for them to assess the risk and return of investments in extractive companies and resource-rich countries. Project-level data in particular allows investors to assess risk that may be obscured in more aggregated data. For instance, risk of bribery or expropriation may vary greatly depending on where a project is, who is involved and the particular geological formation or resource.¹³²

The results from the stakeholder survey confirmed that institutional investors in China and abroad would welcome expanded reporting from resource extractive companies listed on the SSE. Numerous stakeholders in the survey expressed a desire for the SSE's to align its reporting requirements with the Hong Kong Stock Exchange's listing requirements, or to go beyond by requiring annual reporting.¹³³ Such support is congruent with the over 80 institutional investors who officially support the Extractive Industries Transparency Initiative and the dozens of individual and institutional investors who filed briefs in support of Dodd-Frank 1504.

Reduce Company Risks

Imposing reporting requirements on extraction companies listed on the SSE limits them from potential conflicts with resource-rich governments

If listed resource extractive companies are required to comply with strict disclosure standards, it will help to discourage unscrupulous governments from changing the conditions of extractive leases and from demanding unexpected fees and bribes. Reporting according to an international standard allows businesses to reduce

costs and risks that come with following different rules, practices and accounting standards in different jurisdictions.

From the company assessments in this report, it is clear that the majority of the resource extractive companies on the SSE only provide the bare minimum with respect to required information about their international activities. At best, the international payment information companies provide is fragmented, at worst the information is non-existent. If the SSE were to adopt payment disclosure rules, listed companies would benefit from explicit guidance from the SSE about what extractive companies needed to disclose.

Support social harmony by promoting accountable government SSE requirements to disclose payments to governments would give the citizens of resource-rich countries a greater ability to hold their governments accountable

Payment transparency significantly contributes to ensuring that citizens of resource-rich countries can hold their governments accountable for the natural resource revenues received by the government. Reporting on payments on a project-by-project basis provides clear evidence of how companies contribute to government revenues and communities.

Most respondents in the stakeholder survey stated that a lack of transparency in the resource extractive industry hinders citizens in holding governments accountable for their actions. These arguments have been influential in the drive to expand EITI and implement Dodd-Frank 1504 and the European Union's Transparency Directive.

Suggestions for the SSE for immediate action

Resource extractive industry disclosure requirements

- **Standardize sustainability reporting**
We recommend the SSE release detailed guidance on its expectations for the content of a sustainability report (for instance industry specific requirements), including clear definitions of how sustainability performance items should be calculated.
- **Adopt international best practice**
We recommend the SSE to follow international best practice standards and require mainland extractive companies to annually provide details on payments (taxes, fees, royalties, bonuses and other significant payments) to domestic and host governments on a country-by-country and a project-by-project basis.

- **Report on overseas operations**
The SSE should require listed companies to disclose on its overseas sustainability performance including governance, social and environmental aspects.
- **Endorse the Extractive Industry Transparency Initiative**
We recommend the SSE acknowledge the EITI framework, where extractive companies that operate overseas report on payments (including taxes, fees, royalties, dividends, bonuses and other significant benefits) to host governments.
- **Improve guidance on transfer of mining rights**
According to the EITI, companies need to report the bonuses concerning grants and transfers of extraction rights and license fees, rental fees, entry fees and other considerations for licenses and concessions to host governments. The SSE can improve its existing regulation on mining rights by requiring listed extractive companies to disclose the amount they paid for prospecting, exploration and production licenses to host country governments when acquiring and transferring overseas mining rights.

General disclosure requirements

- **Increase clarity on *Social Contribution Value Per Share (SCVPS)***
Several stakeholders have commented that although the SSE's SCVPS is a highly appreciated initiative to quantify corporate impact on society, the formula for how a company calculates its score remains open to interpretation and demands additional clarifications. The SSE should clarify how the SCVPS is calculated. The SSE could also introduce additional items to the SCVPS formula such as environmental recovery expenses, and direct economic losses caused by environmental pollution and overseas operations.
- **Require release of all disclosures made by a company**
According to our company assessments, several companies have disclosed slightly more information about payments to host governments under requirements of the International Financial Reporting Standards (IFRS) or US stock exchanges (20-F form). However, these disclosures did not appear in reports released by Chinese companies listed on the SSE. Also, some companies participated in disclosure initiatives such as the EITI. The SSE could encourage listed companies to re-publish all payments previously disclosed in one comprehensive report.

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