January 18, 2011

# SEC Proposes Rules Implementing Dodd-Frank Disclosure Requirements for Resource Extraction Issuers

The SEC has proposed rules to implement Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act which requires resource extraction issuers to disclose payments made to U.S. or foreign governments for the commercial development of oil, natural gas or minerals. In large part, the proposed rules reiterate the text of the Dodd-Frank provision and do not define many of the key terms in the provision, but do request comment on whether and how to define these terms. Input on these definitions through the comment process could affect the ultimate workability of the rules. We urge companies subject to the proposed rules to express their views on these definitions by contacting us or by commenting to the Commission directly. Comments are due by January 31, 2011.

## Who Would be Subject to the New Rules?

The proposed rules would apply to both U.S. and foreign private issuers that (1) file an annual report with the SEC and (2) engage in the commercial development of oil, natural gas or other minerals, regardless of the size or extent of such commercial development operations. This would include companies that remove the impurities from natural gas after extraction but prior to its transport through the pipeline. It would not include companies engaged in activities that are ancillary or preparatory to commercial development, such as a manufacturer of a product used in the commercial development of oil or natural gas (for example, a manufacturer of drill bits).

## What Type of Payments Would Need to be Disclosed?

Companies subject to the rules would be required to disclose, in an exhibit to their annual report on Form 10-K, 20-F or 40-F, the total amount of payments made by the company or entities under its control to a foreign government or the U.S. federal government for each project related to the commercial development of oil, natural gas, or minerals that is "not de minimis." This would include:

- host government's production entitlement,
- national state-owned company production entitlement,
- profit taxes,
- royalties,
- dividends,
- bonuses,
- license fees, rental fees, entry fees and other considerations for licenses and/or concessions, and
- other significant benefits to host governments.

The proposed rules do not define the term "project" but indicate that this lack of definition would allow companies' flexibility to apply the term in different business contexts. The proposed rules also do not define which payments would be "not de minimis." The SEC indicates in the release that "not de minimis", which is the language in the Dodd-Frank Act, is not a materiality standard and only allows the exclusion of payments so lacking in significance or so minor as to merit disregard. The SEC requests comment, however, on whether it should define "not de minimis" as material or adopt a definition of "not de minimis" that uses a dollar or percentage amount or other specific threshold. The meaning of "not de minimis" in the rules will be a key area of comment. We believe it should be applied as a materiality standard in order to avoid the costly and burdensome provision of immaterial and irrelevant information.

## Potential Conflict with Foreign Laws and Confidentiality Provisions

Unlike other SEC rules, the proposed rules do not contain an exception that would allow companies to exclude payments which may not be disclosed pursuant to foreign laws or confidentiality agreements. The SEC has requested comment, however, on whether such an exception should be included in the rules. This too will be a key area of comment because the absence of such an exception could force companies to choose between complying with U.S. laws and their obligations under foreign laws or contract. The SEC has recognized similar conflicts in the past and allowed for exceptions in limited circumstances, such as in oil and gas reserve disclosures.

## Furnished Rather Than Filed

The disclosure of payments to the U.S. federal or foreign governments will be "furnished" rather than "filed" and therefore will not be subject to liability under Section 18 of the Exchange Act or incorporated by reference into an issuer's Securities Act or Exchange Act reports unless the issuer expressly does so.

## Effective Date

The disclosures would first be required in annual reports relating fiscal years ending on or after April 15, 2012.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact


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