INSPECTION

OFFICE OF
INSPECTOR GENERAL
U.S.DEPARTMENT OF THE INTERIOR

United States' Implementation of the Extractive Industries Transparency Initiative

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INSPECTOR GENERAL
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Memorandum

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To: Greg Gould
Director, Office of Natural Resources Revenue

From: Mary L. Kendall
Deputy Inspector General

Subject: Final Inspection Report – United States' Implementation of the Extractive Industries Transparency Initiative
Report No. 2016-EAU-041

This memorandum transmits the findings of our inspection of the United States' implementation of the Extractive Industries Transparency Initiative (EITI). Our inspection objective was to determine the status of the U.S. implementation of the EITI standard. We are not making any recommendations in this report but are providing it for information purposes only.

The legislation creating the Office of Inspector General requires that we report to Congress semiannually on all audit, inspection, and evaluation reports issued; actions taken to implement our recommendations; and recommendations that have not been implemented.

If you have any questions concerning this report, please do not hesitate to contact me at 202-208-5745.

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Results in Brief

The United States (U.S.) has made significant progress meeting the individual requirements necessary to achieve compliant status with the Extractive Industries Transparency Initiative (EITI). EITI is a global initiative that promotes revenue transparency and accountability for natural resource extraction. The Department of the Interior (DOI) works in collaboration with industry and civil society partners[1] to implement EITI on behalf of the United States.

Our review found that the U.S. has met seven of the eight EITI requirements and partially met one requirement in its effort to achieve EITI compliant status, the highest level of implementation. It has only partially met the revenue collection requirement (Requirement 4) because it has been unable to obtain full disclosure of extractive resource payments from companies, thus preventing the required reconciliation to Government receipts. In addition, the U.S. has encountered challenges as part of its participation in EITI that could prevent it from reaching the goal of compliant status. Should the U.S. not achieve compliant status, its standing in EITI would be diminished.

In spite of the framework laid out in Requirement 4 and the ensuing challenges, the U.S. could still meet this requirement. Through its regular ongoing operations, the U.S. has a system in place that achieves the standard's disclosure and reconciliation requirement, through a process known as mainstreaming. This reporting method may enable the U.S. to meet the EITI reporting and reconciliation mandates without necessarily following the prescriptive language of the standard.

We are not making any recommendations in this report but are providing this document for informational purposes to the Office of Natural Resources Revenue—DOI's EITI representative—and to the members of the U.S. EITI multi-stakeholder group for use as they move forward.

At the close of our field work, senior Government officials disclosed that the U.S. was considering all options associated with the validation process in spite of uncertainties in achieving Requirement 4. We learned that the U.S. is scheduled to undergo validation in April 2018, even though it expects the EITI international board to find that it has made inadequate progress toward validation. If that occurs, the U.S. likely would transition from an implementing country to a country that only supports EITI. The U.S. intends to continue its efforts to disclose revenue and maintain its public website by institutionalizing EITI processes.

[1] Civil society is defined as community and citizenry involvement. In the U.S., it includes academia, non-governmental organizations, and labor unions.

Introduction

Objective

We conducted this inspection to determine the status of the United States' implementation of the Extractive Industries Transparency Initiative (EITI) standard.

Appendix 1 contains the scope and methodology, as well as sites visited.

Background

EITI is a global initiative that aims to promote revenue transparency and accountability for natural resource extraction (e.g. oil, natural gas, coal, non-energy minerals such as gold, and renewable energy). The initiative grew out of concern about corruption and mismanagement of these resources worldwide. Many EITI participating countries are in developing parts of the world, and the initiative seeks to strengthen these government and company systems. The U.S. Government, however, has long had a management system featuring numerous controls and protections to oversee natural resource extraction, which helps reduce the risk of corruption.

As a leading extractive producer of such natural resources as oil, natural gas, and coal, the U.S. announced its intention to join EITI in September 2011. The Secretary of the Interior serves as the Administration's senior official responsible for EITI implementation. The Office of Natural Resources Revenue (ONRR) within DOI serves as the Government's lead representative on the multi-stakeholder group (MSG). The U.S. has been working toward achieving compliant status, and validation is scheduled to begin in April 2018.

To date, DOI expenditures for EITI have totaled approximately $6.5 million, of which the Government spent $2.8 million in fiscal year 2016. The largest expenditures included Government labor and contracts for outside services. Current estimates of expenditures for reconciliation of Government receipts to company payments total $519,000 per year.

The EITI standard has eight primary requirements and multiple subparts that countries must follow when implementing EITI. A synopsis of the eight EITI standard requirements is detailed in Figure 1 below.

EITI Standard Requirements
1: Multi-stakeholder group oversight. Government, industry, and civil society engagement.

EITI Standard Requirements
2: Legal and institutional framework. Disclosure of legal framework and fiscal regime governing extractive industries.
3: Exploration and production. Disclosure of exploration and production activities, as well as export data.
4: Revenue collection. Disclosure and reconciliation of company payments and Government revenues.
5: Revenue allocations. Disclosure of revenue distribution, revenue management, and expenditures.
6: Social and economic spending. Disclosure of social expenditures and the extractive sector's impact on the economy.
7: Outcomes and impact. Disclosure of discrepancies identified in EITI reports, as well as lessons learned during implementation.
8: Compliance and deadlines for implementing countries. Outlines timeframes established by the EITI international board and consequences of noncompliance with the deadlines and requirements for EITI implementation.

Figure 1. A full explanation of EITI requirements is available at https://eiti.org/eiti-requirements.

The initiative is implemented by governments, in collaboration with the MSG, which includes industry and civil society, the latter defined as community and citizenry involvement (e.g. academia and non-governmental organizations). In the U.S., MSG formation in 2012 brought together these three sectors for the first time to achieve a common goal. Initially skeptical, MSG members found that genuine cooperation could generate appreciation for differing viewpoints.

EITI has 56 participating countries. Each country that chooses to implement the EITI standard must establish an MSG that oversees implementation. In addition, most countries, including the U.S., create a national secretariat with a full-time staff to administer the program. The EITI international board, headquartered in Oslo, Norway, is the governing body. Countries implementing the standard publish an annual report in which governments publicly disclose payments received from companies obtaining extractive resources, which an independent administrator reconciles with payments disclosed by those companies.

Countries join EITI with the goal of achieving compliance with the EITI standard. To achieve compliant status, a country must go through the EITI validation process. This includes a comprehensive evaluation of the country's progress toward achieving the eight requirements, as determined by the EITI international board. A country must make satisfactory progress on each requirement in the standard in order to achieve compliant status.

Results

Progress in Complying with EITI

The U.S. has been working on EITI implementation since 2011. It has made significant progress meeting the individual requirements necessary to achieve the highest level of EITI implementation, known as compliant status. Based on our analysis, the U.S. has met seven of the eight requirements and partially met Requirement 4, which necessitates that all Government revenue receipts be reported and subjected to reconciliation. Reconciliation involves comparison of Government receipts to company payments, and explains significant discrepancies between the two. This activity is performed by a third party, known as the independent administrator. The Office of Inspector General (OIG) independently assessed the status of DOI's EITI implementation, as shown in Figure 2.[2]

OIG Assessment of DOI EITI Implementation		
Requirement	**Status**	**Comments**
1 – MSG oversight.	Met	MSG formed, with equal representation by government, industry, and civil society. All required meetings and work products achieved.

[2] The EITI international board is the body that officially determines whether a country has fulfilled the standard, and sets four categories of progress for assessing a country's compliance with each requirement: satisfactory, meaningful, inadequate, and no progress. Our determination of the status does not directly align with those categories identified in the standard. Our assessment was not intended to mirror the board or duplicate any effort. For simplicity, we established our own categories: met, partially met, and not met.

OIG Assessment of DOI EITI Implementation		
Requirement	**Status**	**Comments**
2 – Legal and institutional framework.	Met	Collaborating with the General Services Administration, DOI produced a public website known as the portal, which houses natural resource data along with the electronic version of the annual EITI report. We found that the portal, which went online in December 2015, presents natural resource-related information in a user-friendly format. The international board has recognized the portal as a model for other countries to emulate. Online data portal provides details on allocation of contracts and licenses, with links to Bureau of Land Management and Bureau of Ocean Energy Management websites.
3 – Exploration and production.	Met	Online data portal provides details on fossil fuels, renewable energy, and non-energy minerals, as well as exports of various commodities.
4 – Revenue collection.	Partially Met	Low disclosure of nontax and tax revenues by companies prevent required comprehensive reconciliation of Government revenue receipts to company payments.
5 – Revenue allocations.	Met	Online data portal provides details on all revenue streams, distribution of revenues, and recipients.
6 – Social and economic spending.	Met	Online data portal provides details on extractive sector contributions to the economy.

OIG Assessment of DOI EITI Implementation		
Requirement	**Status**	**Comments**
7 – Outcomes and impact.	Met	Online data portal contains recommendations for addressing reconciliation discrepancies and improving the EITI process. To illustrate extractive industry impacts on local communities, the annual report includes 12 county case studies from across the country, as well as data from 18 states, in an effort to increase public awareness. MSG has actively solicited input from the general public concerning U.S. involvement in EITI. Public interest in EITI is not yet strong, but MSG efforts to obtain outside input and to publish meeting minutes promote EITI's principles of openness and transparency.
8 – Compliance and deadlines for implementing countries.	Met	Deadlines for annual progress reports met, and deadlines for EITI reports surpassed.

Figure 2: OIG's assessment of DOI implementation of EITI requirements.

Challenges in Complying with EITI Revenue Collection Requirement

DOI faces numerous difficulties in trying to meet Requirement 4. Some are less challenging than others, providing opportunities for solutions, while others may offer no alternative course of action.

Voluntary initiative

The voluntary nature of EITI makes full company participation in nontax and tax revenue disclosures difficult to obtain. Companies are not compelled to report revenue and tax data, and do not see the benefit of participation. Consequently, a significant number have chosen not to participate.

U.S. privacy laws

Section 6103 of the Internal Revenue Code (26 U.S.C.) provides for the confidentiality of tax returns and return information. It prevents the U.S. Internal

Revenue Service (IRS) from disclosing returns and return information unless the taxpayer authorizes the release or one of several exceptions are met.

Low company participation

EITI Requirement 4 calls for comprehensive disclosure and reconciliation of company payments and Government revenues from extractive industries. Companies make payments to the U.S., and the payments are considered revenues when collected.

In the U.S., revenues associated with extractive industries consist of two categories—nontax and tax. Nontax revenues are comprised of 11 revenue streams (e.g., royalties, bonuses, rents, inspection and permit fees, and civil penalties), whereas tax revenues represent corporate income tax payments reported to the IRS.

Requirement 4 presents a major challenge for the U.S. because of the numerous companies that operate on Federal lands and large sums of revenue involved. Specifically, more than 3,000 companies paid the Federal Government $12.64 billion and $7.80 billion in nontax extractive revenue for the 2015 and 2016 reports, respectively. Since full company participation in the initiative would have been too time consuming and costly to accomplish, the MSG decided to select a manageable sample of companies. This required establishing materiality thresholds, as the standard allows, for company reporting and subsequent reconciliation. The MSG found that a significant and achievable sample of companies could be selected by setting the threshold at $50 million and $37.5 million of total annual revenue reported to ONRR by a parent company, including its subsidiaries, for 2015 and 2016. The threshold amount varies yearly due to changes in commodity prices, which in turn affects the amount of payments made to ONRR. For nontax revenues, this reduced the 3,000 company universe to 45 companies for the 2015 annual report, and 41 companies for the 2016 report. For tax revenues, the sample became 41companies for the 2015 report, and 38 companies for the 2016 report. The number of companies can change from year to year due to factors such as mergers, acquisitions, and bankruptcies.[3]

Unfortunately, a significant number of companies that were asked to participate declined the request, and so the amount of revenues actually reported and reconciled were far less than the 80 percent target (see Figure 3).[4] We determined the U.S. has only partially met Requirement 4. Since the EITI standard requires comprehensive company disclosure, this low level of company participation is of concern as the U.S. seeks validation.

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[3] Companies chosen for participation represent the largest producers of oil, gas, coal, and hard rock in the U.S., including, among others, ExxonMobil Corporation, Chevron Corporation, Shell E&P Company, Arch Coal, Inc., and Peabody Energy Corporation.

[4] Although the target for reconciling tax revenue was all the companies asked to participate in EITI, the U.S. did not report the total amount of tax revenue because companies are not required to disclose this information.

Results From Companies Subject To Reconciliation (Dollars in Billions)				
Report Year	**Nontax**		**Tax**	
	Target	**Achieved**	**Target**	**Achieved**
2015				
Number of Companies Disclosed	45	31 (69%)	41	12 (29%)
Number of Companies Reconciled	45	31 (69%)	41	5 (12%)
Revenues Reconciled	$10.44	$8.50 (81%)		
2016				
Number of Companies Disclosed	41	25 (61%)	38	12 (32%)
Number of Companies Reconciled	41	25 (61%)	38	7 (18%)
Revenues Reconciled	$6.11	$4.83 (79%)		

Figure 3. Information about companies not disclosing their payments. In the tax column, the target for revenues reconciled could not be established and reconciled because most companies did not report tax data. The independent administrator reconciled all of the revenue that companies reported, but the reconciliation did not reflect the target revenues.

Subnational reporting

The EITI standard requires that MSG establish whether or not direct payments from companies to subnational government entities (states and tribes in the U.S.) are significant.[4] If significant, then disclosure and reconciliation of payments to these entities are included in the EITI report. Given significant practical barriers to collecting data from all 50 states, the MSG focused its efforts on 18 states with the most extractive revenue.

To date, only three of these 18 states have chosen to disclose data about their extractive industries. These three still have not agreed to reconcile company payments to Government receipts. Further, since U.S. law recognizes tribes as

[4] Subnational is defined as below the national Government level—in the U.S. this refers primarily to state and tribal governments.

sovereign nations, they are not bound to participate in EITI, and no tribes have volunteered for this purpose.

Although the U.S. received approval from the EITI international board to deviate from full subnational reporting for past reports, it has no guarantee that this approval will continue in the future. The U.S. EITI MSG endorsed a renewed request to deviate from subnational reporting, which it submitted to the international board in December 2016.

Beneficial ownership

As of January 2020, the standard requires disclosure of beneficial ownership information in the EITI report. Beneficial ownership refers to individuals who directly or indirectly own or control a corporate entity.

In December 2016, the U.S. published its "roadmap" or plan for meeting the future beneficial ownership disclosure requirement. Collection and disclosure of this information may prove problematic, however, since the U.S. does not have an institutional structure for public disclosure of beneficial ownership, and voluntary participation may produce limited results. For example, DOI does not have any mechanism to collect beneficial ownership information when conducting lease sales related to extractive industry operating rights on U.S. Federal lands or for regulating extractive operations, as well as collecting production related fees and royalties.

Mainstreaming

Mainstreaming is a mechanism through which countries disclose revenue collection, accounting, and disbursement as part of routine Government operations. It is advantageous for two reasons – first, it highlights countries that make transparency an integral and routine feature of their management systems. Second, countries that achieve mainstreaming do not have to undergo the reconciliation process. To achieve mainstreaming, the U.S. must submit to a rigorous application process, which is subject to approval by the international board.

We found the U.S. is actively pursuing mainstreaming to satisfy Requirement 4 by reporting that it routinely discloses 100 percent of all nontax revenue streams. In addition, the U.S. is preparing a thorough description of its robust audit processes and procedures for the 2017 annual report. Among these are the following—

- ONRR and its State and tribal partners help ensure that companies pay correctly through the use of audits, compliance reviews, data mining, and an enforcement program;
- ONRR accounts for nontax revenues using company-submitted royalty reports—more than 150 up-front automated edits of these reports help detect irregularities;
- Bureau of Land Management and Bureau of Safety and Environmental Enforcement conduct physical inspections of lease operations;

- An independent accounting firm annually audits DOI's financial statements, which include extractive revenue;
- DOI and DOI's bureaus are independently audited by the Office of Inspector General, and IRS receives audit oversight from the Treasury Inspector General for Tax Administration; and
- IRS verifies tax payments made by companies.

These processes and procedures ensure accountability for 100 percent of natural resource revenues. Accordingly, the U.S. could be in compliance with Requirement 4, even if full reporting and reconciliation from the EITI international board is considered questionable. Although mainstreaming could be a possible solution to demonstrate that the U.S has complied with Requirement 4, the request has not yet been approved by the international board. Further, it is questionable whether or not the international board would grant such approval. Also, the U.S. still has work left to accomplish in order to develop the contextual narrative of its audit processes and procedures in a manner that fully demonstrates compliance with Requirement 4.

At the close of our field work, Government senior officials disclosed that the U.S. is considering all options regarding validation. It expects to produce its third annual report in December 2017 and undergo validation in April 2018. Although it has met 7 out of 8 requirements it expects not to be found in compliance with the EITI standard until companies follow through on EITI reporting requirements outlined in Requirement 4. Instead, the U.S. will move from being an implementing country to only a supporting country of EITI. Nevertheless, the U.S. intends to continue its efforts to disclose revenue and maintain the online data portal, thus institutionalizing EITI processes.

Appendix 1: Scope and Methodology

Scope

Our inspection examined the activities of the United States' implementation of the Extractive Industry Transparency Initiative (EITI) since 2011.

Methodology

We conducted this review from June 2016 through March 2017. During our inspection, we—

- reviewed relevant laws, regulations, policies and procedures concerning U.S. EITI implementation;
- reviewed and analyzed data and documents, both hardcopy and electronic;
- reviewed the EITI standard and requirements;
- attended two multi-stakeholder group meetings;
- interviewed representatives from the EITI international board's secretariat and U.S. Department of State;
- interviewed key members of Government, industry, and civil society sectors;
- interviewed the Director of the Office of Natural Resources Revenue (ONRR) and key agency staff with EITI responsibilities; and
- interviewed key representatives from the independent administrator, Deloitte Touche, LLP.

We visited—

- ONRR offices in Washington, D.C., and Lakewood, CO; and
- Deloitte Touche, LLP, in Arlington, VA.

We did not test operation and reliability of internal controls related to U.S. EITI. We were provided with computer-generated data related to EITI expenditures, which we used but did not test for completeness and accuracy.

We conducted this inspection in accordance with the Quality Standards for Inspection and Evaluation as put forth by the Council of the Inspectors General on Integrity and Efficiency. We believe that the work performed provides a reasonable basis for our conclusion.

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