Client Alert

June 16, 2015

Canada's New Extractive Sector Transparency Measures Act and its Implications for Companies Subject to the U.S. Foreign Corrupt Practices Act

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On June 1, 2015, Canada's Extractive Sector Transparency Measures Act ("ESTMA" or "the Act") came into force. Approved in December 2014, but not in force until this month, the Act requires companies in the extractive sector to report annually on certain payments made to any level of government—including payments made to employees of state-owned corporations—both in Canada and abroad. In line with Canada's commitment to join global anti-corruption efforts, the Act's stated purpose is to enhance transparency in the resource extractive sector in order to deter and detect corruption, including corruption under Canada's Corruption of Foreign Public Officials Act. As discussed in this client alert, the Act contains its own enforcement and penalty provisions. Equally important, in light of the heavy scrutiny given to the extractive sector by foreign bribery prosecutors—according to a recent study by the Organization for Economic Co-operation and Development (OECD), 19% of all concluded foreign bribery cases since 1999 have involved the extractive industries—the Act also has broader implications for foreign bribery enforcement, including enforcement of the U.S. Foreign Corrupt Practices Act (FCPA). Indeed, consistent with the OECD study, a significant number of FCPA enforcement actions have implicated the extractive sector, including the TSKJ cases, which involved bribery in the liquefied natural gas industry and resulted in the largest combined FCPA resolution in history.[1] Accordingly, Canadian extractive companies and companies doing business in Canada that are involved in the extractive sector should pay close attention both to the requirements of the ESTMA itself and to its potential impact on anti-corruption enforcement efforts.

APPLICATION

The ESTMA applies to businesses engaged in the commercial development of oil, gas, or minerals that are either (a) listed on a stock exchange in Canada, or (b) doing business in Canada and meet two of three size-related criteria in one of their two most recent financial years:

- at least CAD $20 million in assets (USD $16.2 million)
- at least CAD $40 million in revenue (USD $32.4 million)
- employs an average of at least 250 employees

[1] TSKJ was the name of a four-company joint venture formed in 1990 for the purpose of bidding on engineering, procurement, and construction contracts to build liquefied natural gas facilities on Bonny Island, Nigeria. The U.S. Department of Justice and U.S. Securities and Exchange Commission brought multiple enforcement actions in connection with a scheme to pay bribes to Nigerian government officials on behalf of TSKJ, including against the four companies that formed the joint venture.

Importantly, for companies in the latter category, the Act does not specify whether the assets, revenue, or employees themselves must be located in Canada, or whether the business being done in Canada must itself be related to oil, gas, or mineral development. Thus, a large multinational corporation doing business in Canada in the non-extractive sector might still be covered by the Act if it conducts activities related to oil, gas, or mineral development elsewhere in the world.

There may be some relief for such multinational companies, however, as the Act provides for the possibilities that (a) a parent's report may be deemed sufficient to satisfy the obligations of a wholly owned subsidiary and (b) a report filed in another jurisdiction may be deemed to satisfy Canada's reporting requirement if the Minister of Natural Resources[2] determines that "the requirements of the other jurisdiction are an acceptable substitute" for Canada's requirements. In this regard, it is notable that both the United States and the European Union require analogous reporting, although these reporting regimes generally have not been fully implemented.[3] It is also an open question as to how Canada, or any of the other jurisdictions, will deal with potential conflicts between the extractive sector disclosure requirements and data privacy laws.

REQUIREMENTS

The ESTMA requires reporting entities to report annually on "payments" in the aggregate of at least CAD $100,000 (approximately USD $81,000) made to a "payee" for each financial year beginning after June 1, 2015. The Act authorizes the Minister to specify the way in which payments are to be organized or broken down in the report, including on a project basis, but the Minister has yet to issue such specifications.[4] The reports must include an attestation made by a director or officer of the entity, or an independent auditor or accountant, that the information in the report is true, accurate and complete. The reports must be filed no later than 150 days after the end of the company's financial year and must be made publicly available, such as through the company's website.

The ESTMA also requires reporting entities to keep records of payments made in a financial year for a seven-year period (unless otherwise specified). Under the Act, the Minister may order the reporting entity to provide any information or documents, including (among other examples) a list of projects for the commercial development of oil, gas, or minerals in which the entity has an interest and the nature of that interest, the results of an audit of its report, or the records of payments for the financial year to which the report relates. Further, a person designated by the Minister may, for a purpose related to verifying compliance with the Act, enter any place in which the person has reasonable grounds to believe there is anything to which the Act applies or any document relating to the administration of this Act. The Act delineates the designated person's powers upon entry, which include examining anything in the place, including any document or data contained on any computer system.

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[2] Section 5 of the Act dictates that the Governor in Council, may, by order, designate a member of the Queen's Privy Council for Canada as the Minister for the purposes of this Act. According to an Order in Council dated May 15, 2015, the Governor in Council designated the Minister of Natural Resources to be the Minister for the purposes of this Act.

[3] In 2012, the U.S. Securities and Exchange Commission (SEC) promulgated its extractive sector disclosure rules, as required by section 1504 of the Dodd-Frank Act, but they were invalidated by the U.S. District Court for the District of Columbia in 2013. The SEC is currently working on revised proposed regulations. In the European Union, the Accounting and Transparency Directives have been implemented in the UK, with the passage of the Reports on Payments to Governments Regulations 2014. The UK is the first European Union member state to implement the Accounting and Transparency Directives, but other member states are expected to follow suit later this year. A similar law in Norway, which is not a member of the European Union, went into effect on January 1, 2014.

[4] Similarly, the Minister has not issued other regulations as authorized under the Act.

Below we explain the potential FCPA implications of some of the Act's provisions.

CONVERGENCE WITH THE FCPA

The ESTMA defines the term "payee" broadly to include not only the Canadian and foreign governments, or any body established by multiple governments, but also "any trust, board, commission, corporation or body or authority that is established to exercise or perform, or that exercises or performs, a power, duty or function of government for" such governments. Thus, not only payments to an oil ministry but also payments to a national oil company, for example, could fall within the reporting requirement. Such state-owned corporations can be considered "instrumentalities" of a foreign government under the FCPA. Moreover, the Act provides that "a payment that is made to an employee or public office holder of a payee is deemed to have been made to the payee." Payments to employees of state-owned enterprises often form the basis of FCPA enforcement actions. By requiring disclosure of payments made to officers and employees of government entities, including state-owned corporations, the Act could require companies to publicly identify payments made to individuals deemed to be "foreign officials" for purposes of the FCPA—which could draw the interest of U.S. authorities.

Illicit payments to foreign officials are often disguised as consulting payments, sales commissions, or other types of third-party payments. It is not clear from the face of the ESTMA whether all such payments would fall within the scope of the reporting requirement. This is because the Act specifically restricts the definition of "payment" in terms of scope and type. First, to fall within the Act, the payment must be "in relation to the commercial development of oil, gas or minerals." Second, the payment must also fall within one of eight specified categories:

- taxes, other than consumption taxes and personal income taxes;
- royalties;
- fees, including rental fees, entry fees, and regulatory charges as well as fees or other consideration for licenses, permits, or concessions;
- production entitlements;
- bonuses, including signature, discovery, and production bonuses;
- dividends other than those paid to governments as ordinary shareholders;
- payments for improvements in infrastructure; and
- any other prescribed category of payment.

To date, there have been no other categories of payments prescribed. It is not readily apparent whether a consulting payment or a sales commission would fall within one of these eight categories, even if they were made "in relation to the commercial development of oil, gas or minerals." Nevertheless, the Act does contain certain provisions that seem to be designed to avert the concealment of the true nature of a payment. In particular, the Act provides that "a payment that is due to a payee and that is received by a body that is not a payee for the payee is deemed to have been made to the payee." This language would seem to address payments made to foreign officials "indirectly" (in FCPA parlance) through the use of third-party intermediaries. Moreover, the Act defines "payment" to include both monetary and in kind payments, meaning that gifts, travel, and entertainment provided to an official could fall within the scope of the reporting requirement. Thus, the Act potentially covers two key areas—payments to third-parties and gifts, travel, and entertainment—that frequently form the basis of FCPA enforcement actions. However, as noted above, any such payments would still need to fall within one of the eight specified categories to trigger the reporting requirement.

The ESTMA contains additional safeguards designed to prevent companies from avoiding the reporting requirements by making separate payments of less than $100,000 each. First, the reporting requirement is triggered by the making of payments within a specified category in "the total amount" of CAD $100,000. Second, the Act specifically prohibits structuring payments, whether in monetary or in kind, "with the intention of avoiding the requirement to report those payments, obligations, or gifts in accordance with this Act."

ENFORCEMENT, PENALTIES, AND DEFENSES

The ESTMA provides that the Minister of Natural Resources may order an entity "to take measures that he or she considers to be necessary to ensure compliance with" the Act's reporting and public accessibility requirements. The ESTMA also provides for both corporate and individual criminal liability for:

- failing to truthfully report relevant payments;
- failing to make such reports available to the public;
- structuring payments to avoid the reporting requirements;
- failing to keep records of payments for the requisite seven-year period; and
- engaging in certain obstructive conduct such as failing to produce or provide access to certain requested information, failing to assist a designated person in the exercise of his or her duties or otherwise obstructing or hindering a person who is exercising powers or performing duties or functions under the Act, or making false or misleading statements or providing false or misleading information to the Minister or his or her designee; and
- failing to comply with a corrective order.

The Act expressly creates corporate liability for the acts of the corporation's employee, agent, or mandatary and does not require that any such individual be specifically identified or prosecuted for the underlying offense.

An entity or person that fails to comply with the Act's requirements will be guilty of an offense punishable on summary conviction and liable for a fine of up to CAD $250,000 (approximately USD $203,000). The Act further provides that an offense that is committed or continued on more than one day constitutes a separate offense for each day on which the offense is committed or continued.

Significantly, the ESTMA incorporates an affirmative defense, which provides that persons or entities will not be found guilty if they establish that they exercised "due diligence" to prevent the commission of the offense. Because the Act does not expressly define due diligence, companies should follow best practices in compliance and internal accounting controls in order to potentially gain protection under this defense.

KEY TAKEAWAYS

- The purpose of the ESTMA is to increase transparency and decrease corruption in the extractive industry. By its very nature, then, the Act creates the potential for more anti-corruption enforcement, not only by Canadian authorities but also by other countries, including enforcement under the U.S. Foreign Corrupt Practices Act. By mandating the public disclosure of large payments in high-risk jurisdictions and in high-risk industries, the Act could result in drawing the attention of law enforcement agencies to certain payments that may previously have gone unnoticed. Because the Act requires disclosure of certain payments to employees of state-owned companies in relation to the commercial development of oil, gas, or minerals, it will necessarily require the disclosure of the types of payments that have served as the basis for many FCPA enforcement actions in the past—such as the TSKJ cases, which, as noted above, involved the extractive sector and resulted in the largest combined FCPA penalty of all time. Moreover, by providing the Minister of Natural Resources or his or her designees with the authority to inspect a company's books and records, the Act provides an opportunity for Canadian authorities to scrutinize a company's internal accounts and correspondence and to discover potentially improper payments even if they weren't disclosed. Indeed, we have seen FCPA enforcement actions, such as the *Direct Access Partners* cases, that had their genesis in routine administrative examinations. Given the historically cooperative ties between Canadian and U.S. law enforcement authorities, and their respective obligations to assist each other in foreign bribery investigations and proceedings under the OECD Anti-Bribery Convention, this could result in parallel investigations under both Canada's Corruption of Foreign Public Officials Act and the FCPA. In short, the Act increases the likelihood of extractive-sector-focused anti-corruption investigations, in Canada, in the United States, and farther abroad.

- Domestic and foreign entities exploring for or extracting oil, gas, or minerals directly or through their subsidiaries, and having a nexus with Canada, should determine whether the ESTMA's requirements are applicable. If so, reporting entities should review and update their compliance programs and internal accounting controls consistent with the Act's requirements. Companies should consider the following practices, among others:

    - Implementing a robust system of internal accounting controls designed to track and record payments made to the types of governmental entities enumerated in the Act, to identify when such payments were made in connection with the commercial development of oil, gas, or minerals, and, potentially, to assign these payments to specific projects;

    - Auditing payment records to ensure the accuracy and completeness of such records and to determine whether appropriate revisions to the compliance program or internal controls need to be made;

    - Updating or implementing policies, including, for example, record retention policies, for the purpose of meeting the Act's obligations; and

    - Training relevant officers, employees, and agents as to the requirements of the ESTMA, including, among other things, the types of payments covered by the Act, the record-keeping requirements, and the prohibition on structuring payments to avoid the reporting requirements.

In light of the potential criminal liability for a false attestation, measures such as these should give some comfort to any officer or director tasked with attesting to the report and should also assist a company in the event that the Minister orders an audit of the company's compliance with the Act. Moreover, although the Act does not specifically define what amount or type of "due diligence" is required to establish a defense to liability, by implementing these and other reasonably prudent measures, a company will be well positioned to invoke that defense or to otherwise argue for a lesser sanction (e.g., the issuance of a corrective order instead of summary conviction, or a reduced penalty). Such measures will also be viewed favorably by U.S. authorities in the event of an FCPA investigation.

- The enactment of the ESTMA is part of a larger global trend to champion greater transparency and accountability within the extractive sector. Companies should monitor developments in this area closely as new (and similar) legislation will likely emerge in even more jurisdictions worldwide. Moreover, to take advantage of "substitution" provisions such as those available under the ESTMA, companies should develop policies, procedures, and controls designed to satisfy the reporting requirements of multiple jurisdictions.

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