20TH EITI BOARD MEETING LIMA, 27-28 JUNE 2012

EITI International Secretariat Oslo, 8 June 2012

Board Paper 20-2 A

EITI Strategic Options

For discussion and decisions

Summary

The attached paper contains proposals for the strategic evolution of the EITI.

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COVER NOTE

1. The attached paper contains proposals for the strategic evolution of the EITI, suggestions on how the Board might wish to examine these proposed changes and some background information on the process so far.

2. The proposal put forward in the paper has two interrelated elements: (1) **strengthening and clarifying the existing requirements for EITI implementing countries**; and (2) **redesigning the EITI's validation system**. The clarification of the requirements and the redesign of the validation system need to be considered together, as the way in which performance is assessed will have an impact on performance itself. It is therefore not possible to first in isolation consider what the EITI requires without at the same time considering how the meeting of these requirements will be assured.

3. A separate attachment (Strategy consultation plan) outlines the EITI's plans for consulting its stakeholders on the proposed changes. It is an update of the document that was initially shared ahead of our meeting at Wiston House as is available on the EITI website.

Strengthening and clarifying the existing requirements for EITI implementing countries

4. As directed by the Strategy Working Group, the attached paper includes **proposals on issues that the group agreed ought to become new or modified minimum requirements**, including:

- that EITI reports must contain background information on the extractive sector/s;
- clarifying the language in the requirements with regards to direct subnational payments;
- modifying the requirements related to in kind revenues and state owned enterprises;
- requiring disclosure of licenses and license-holders, including beneficial ownership; and
- company-by-company reporting of each revenue stream.

5. There are a number of additional issues where the SWG concluded that further discussion is needed, including:

- local content;
- midstream payments;
- licensing (elements beyond disclosure of licenses and beneficial ownership);
- contracts;
- project-level reporting; and
- social expenditures.

The attached paper sets out options for the Board to consider (i.e., whether these proposals should become new or modified requirements, an option mentioned in the EITI Rules, or an option available to MSGs but not mentioned in the EITI Rules).

6. The present 21 requirements are overlapping, repetitive, not necessarily sequential, and mix up process with outcomes. The Secretariat recommends **a revision of the requirements** so that they are presented more concisely, clearly and in a more outcomes-focused manner. (For example, they might be distilled to the following six aspects: the

timeliness of the data, the comprehensiveness of the data, the reliability of the data, the explanation of discrepancies, the functioning of the MSG and the communication and dissemination of the data). The revised version of the requirements would also encourage MSG to consider optional elements that can add value to the EITI process.

Redesigning the EITI's validation system

7. As directed by the Strategy Working Group, the attached paper also includes a proposal by the International Secretariat on **a new quality assurance system to replace the current validation system**. The Secretariat's proposal has two elements: one focused on measuring compliance with the EITI requirements (numerical scoring) and the other focused on assessing implementing counties broader efforts to realise the EITI principles (alphabetical scoring).

8. The numerical system would be based – as today – on assessing whether a country has met the EITI requirements. As indicated above, this process would be strengthened by a clearer articulation of the requirements. It is suggested that the modified validation system moves beyond the current pass/fail approach, by acknowledging progress toward compliance, and recognise where countries have exceeded the minimum requirements.

9. Further work needs to be done on such a modified quality assurance arrangements (new validation system), in particular on the suggested alphabetical scoring. There are three key aspects that the Board is recommended to consider relating to the proposed alphabetical scoring :

- That it be non-comparable and based on country's own work plans and targets.
- That it be based on how the MSG seeks to deliver on EITI's wider principles.
- That it be assessed by an Expert Panel for a recommendation to the Board.

Next steps

10. Once the Board has broadly agreed on how to address these various aspects, detailed requirements and guidelines would have to be developed. Based on what is agreed in Lima, it is therefore envisaged that a drafting process would commence shortly afterwards, developing proposals that the Board could approve in the autumn. While the Strategy Working Group has yet to consider drafting aspects of changes to the EITI standard, it is noted that the working group on theory of change has suggested a greater focus on whether the EITI delivers the desired outcomes and a study by the Chartered Institute of Public Finance & Accountancy (CIPFA) recommends that criteria 2 and 3 needs significant revising to address some of the shortcomings with current implementation. It is therefore possible that the EITI Rules would need more substantial redrafting, with the criteria modified and/or some core requirements identifying desired outcomes, followed by more detailed guidance on delivery and quality assurance. None of the changes to the EITI Rules would come into force until the Board agrees a new version of the EITI Rules, including transitional arrangements for existing implementing countries, for adoption at the 2013 EITI Conference.

Background

11. In Amsterdam in June 2011, the Board agreed that there was a need to carefully consider the EITI's strategic options and decided to establish a Strategy Working Group. All stakeholders were invited to contribute. In Bangka in October 2011, following a review of a

number of submissions, the Board agreed that the Chair would convene a small group of representatives to prepare an options paper. Board Paper 19-10-B was discussed at Wilton Park in February 2012.

12. There was wide agreement that the EITI standard needs to evolve, both by strengthening the EITI standard and by incentivising implementing countries to link the EITI with other reform efforts and to go beyond what is required. The Board considered several options for refining the validation system beyond a pass/fail approach to compliance. It was agreed that two working groups would be set up to build on the work of the group that developed the options paper: one group would discuss improvements to the EITI within its current parameters and the other will discuss additions to the scope of the EITI. These groups were tasked with preparing proposals for consideration at the next Board meeting, in Lima in June.

13. The two groups, together forming the Strategy Working Group met in Henley outside London on 11-12 April. The participants considered a wide range of proposals for the future direction of the EITI. The background papers for the meeting are available online . The group broadly agreed recommendations and identified options for consideration by the Board in Lima. It was agreed that the Secretariat would compile the attached paper, reflecting the discussion and agreements reached, generally setting out proposals or options where further discussions were considered necessary. This paper was circulated to the group for comment in late May, but it has not been endorsed by the members of the Strategy Working Group. Rather, it is reflecting the Secretariat's understanding of the agreements reached.

EITI STRATEGIC OPTIONS

Table of Contents

1. Strengthening and clarifying the existing requirements for EITI implementing countries

1.1 Proposals from the Strategy Working Group

As directed by the Strategy Working Group, the following sections of this paper outlines proposals on issues that the group agreed ought to become new or modified minimum requirements, including:

- that EITI reports must contain background information on the extractive sector/s;
- clarifying the language in the requirements with regards to direct subnational payments;
- modifying the requirements related to in kind revenues and state owned enterprises;
- requiring disclosure of licenses and license-holders, including beneficial ownership;
- company-by-company reporting of each revenue stream
- revising the requirements regarding data quality / reliability; and
- making EITI data more accessible through the development of an EITI data standard, and providing EITI data in an electronic format;.

There are also a number of additional issues where the SWG concluded that further discussion is needed, including, but not limited to:

- local content;
- midstream payments;
- licensing (elements beyond disclosure of licenses and beneficial ownership);
- contracts;
- project-level reporting; and
- social expenditures.

There is a further proposal from the Working Group on Theory of Change about improving the guidance to MSGs on workplans.

The paper sets out these proposals in turn for consideration by the Board. Where an issue is uncontroversial, or where there appears to be an emerging consensus for change, the Secretariat has put forward a specific recommendation for consideration by the Board. Where there are divergent views, the paper sets out the options available to the Board, i.e., new or modified requirements, an option mentioned in the EITI Rules, or an option available to MSGs but not mentioned in the EITI Rules.

There are also a number of issues that have been proposed by EITI stakeholders during the consultation process[1], including:

- revenue allocation (i.e. government allocations of extractive revenues prior to the budget, such as sovereign wealth funds or other front-line deductions)
- efficiency of extraction
- efficiency of expenditure
- full financial reporting on costs and profits.

Board Members may wish to table additional proposals.

Proposal 1: Background information on the extractive sector is included in EITI reports.

It is recommended that background information is required to be included in EITI Reports, including information on production, the licensing and fiscal regime, and the sector's contribution to the economy. Background

This proposal would build on the existing requirement that EITI reports are "comprehensible and publicly accessible in such a way as to encourage that its findings contribute to public debate" (Requirement 18). For additional information refer to:

- Background information on the extractive sector for EITI Reports

Proposal 2: Company-by-company reporting

It is recommended that disaggregated reporting by company and revenue stream is required by implementing countries.

Background

The majority of EITI reports are disaggregated by company and revenue stream. It is currently a requirement that the multi-stakeholder group agrees the degree of aggregation or disaggregation of data in the EITI report (Requirement 9-c-v). For additional information refer to:

- Disaggregation by company

Proposal 3: Project-by-project reporting

It is suggested that the Board considers the following options:

i. Project-by-project reporting becomes a minimum requirement;
ii. Project-by-project reporting is encouraged, but not required; or
iii. Project-by-project reporting is not referred to by the EITI Requirements.

Background

Where project-by-project reporting has been adopted, including in Burkina Faso, Indonesia,

[1] See www.eiti.org/about/strategy-review

Mali and Timor Leste, EITI reports provide disaggregated data at the level of individual payment types and individual production units. Companies are required to submit reporting templates for each of the projects they are involved in. A list of concession-level contracts, leases, PSAs etc., the participating companies, government revenue collection entities, and respective shareholdings is also disclosed. Some stakeholders have argued that project-by-project data would help promote greater transparency and accountability, particularly at the local level. Other stakeholders noted the difficulties in defining a "project", and that some taxes are levied at the national level.] For additional information refer to:

- Project level reporting

Proposal 4: Payments and revenues at sub-national level

It is recommended that disclosure of direct material payments and revenues at subnational level is required (Requirement 9-d, 9-e and 11-d).

Background

While the majority of revenues from the extractive sector accrue at the national level, some payments are made directly from companies to subnational levels. These payments often represent significant income for regions or districts with prominent extractive industry activity. An increasing number of reports include direct payments and revenues collected at sub-national level, including the reports in Ghana and Mongolia. It is currently a requirement that the multi-stakeholder group takes steps towards disclosure of sub-national payments and revenues where material (Requirement 9-e). In Henley, it was agreed that this requirement requires further clarification, particularly with respect to direct payments from companies to local governments.

In addition, multi-stakeholder group is encouraged to report on subnational transfers, in particular where such transfers are mandated by a national Constitution or statute. It is recommended that this requirement remains optional, and that further guidance on including such transfers in EITI reporting is developed. For additional information refer to:

- EITI reporting by subnational governments

Proposal 5: Contracts

It is proposed that the Board considers the following options:

i. Contract disclosure becomes a minimum requirement;

ii. The disclosure of key contract terms becomes a minimum requirement;

iii. Contract disclosure is encouraged, but not required;

iv. Contract disclosure remains optional.

Contract disclosure could include that implementing countries be required to disclose, on a single government website:

- all contracts that govern the government's relationships with oil, gas and mining companies that make material payments.

- Any annex, addendum or side agreement that is part of the core issues covered by the contract;

- Any law, ruling or regulation that affect the core issues of the contract
- disclosure of new contracts be encouraged, even where no payments are yet made nor due during the fiscal period in question.

Background

Contracts detail the commitments between government and companies that determine the payments and revenues from natural resource extraction. Contract disclosure enables users of EITI reports to compare revenue data with financial terms, including incentives, government share in a project, social and environmental provisions etc. of a contract. In some implementing countries, including the Kurdish region of Iraq, Mauritania, Peru and Timor Leste contracts are made publically available or disclosure is provided for in legislation and codes.

The approach adopted by the IFC is often cited. As of May 2013, extractive sector projects financed by the IFC will require the public disclosure of the principal contract between a company and the relevant government, with appropriate redactions of commercially sensitive information. In lieu of full contract disclosure, a company will also be allowed to publish a summary of the key terms and conditions of the relevant contract[2]. For additional information refer to:

- Contract transparency

Proposal6: Transparency of Licenses, license holders and licensing rounds

It is proposed that disclosure of licenses, license holders and licensing rounds is required, and that EITI reports could contain

i. A record of licenses and license holders, including

- **Type, location and commodity;**
- **Date/type of allocation;**
- **Expiry date;**
- **Reserves/production;**
- **Signature bonus due/paid;**
- **Operator, other partners and respective per cent interest;**
- **Ultimate beneficial owner;**
- **Date interest acquired; and**

[2] http://www1.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/IFC+Sustainability/Sustainability+Framework

- o **Any factors affecting the license.**

ii. A record of licensing rounds, including

- o **Company name;**
- o **Ultimate beneficial owner;**
- o **Licence(s) bid for;**
- o **Identity of the government agency that prequalified the company, including compliance with technical and financial criteria;**
- o **Bid parameter 1, 2 etc; and**
- o **Outcomes and reason for outcome.**

Background

License transparency provides users of EITI reports with a record of the award of extractive rights to companies, or changes in ownership to such rights. This enables citizens to examine which companies have been awarded rights to exploit their natural resources and on what basis. Mongolia's 2010 EITI report includes an overview of licenses and license holders, noting licenses issued, purchased or expired during the course of the fiscal period. One option would be to require or encourage annual declarations on changes of ownership (this could be done with or without information on the price, depending on whether this is considered to be commercially sensitive information). For additional information refer to:

- Licenses and the allocation of licenses
- Transparency in licensing and auctioning

Proposal 7: In-kind revenues

It is recommended that disclosure of payments and receipts from state oil/gas export sales is required.

Reporting on oil/gas sales could include that

- **Government entities, including SOEs, disclose revenue received from the export sale of their production share and in-kind revenues, including disclosure of price, grade, volume, date of export and buyer for each cargo sold;**
- **Companies disclose the payments for each cargo bought, including disclosure of price, grade, volume and date of export for each cargo sold.**
- **Disclosure of data by shipment be encouraged, including shipment number, contract number, invoice number and data, quantity, price, loading port and data, quality of crude, destination, due date, settlement and vessel name.**
- **Implementing countries are encouraged to adopt similar reporting mechanisms for domestic oil sales.**

Background

Disclosure of payments and revenues from government export sales enables users of EITI reports to see how much the government earns from the sale of oil, gas and minerals that they receive in-kind in terms of profit oil, royalties, service contracts etc. Iraq's EITI report discloses export sales. While it is currently a requirement that material payments and revenues made in-kind are disclosed, countries are not required to disclose the revenues received from the sale of these in-kind products. For more information refer to:

- In-kind revenues

Proposal 8: State-owned enterprises (SOEs)

It is recommended implementing countries with state-owned enterprises are required to disclose all material revenues received by the SOE and all material transfers made by the SOE to other government entities.

It is proposed that countries be encouraged to disclose additional information on SOEs, including

- **Annual reports and independent audits of SOEs**
- **Production volumes and reserves by license**
- **Equity holding, sale and purchase of shares**
- **Detailed statement of costs, balance sheets**
- **Financial transfers among affiliated companies and subsidiaries within the umbrella of the SoE**
- **Detailed breakdown of expenditures for non-core activities, including social spending and other quasi-fiscal activity**

Background

It is currently a requirement that material payments made by SOEs or material revenues collected by SOEs on behalf of the state are disclosed (Requirement #9 and #11). Disclosure of transfers is not required, although reports from Albania, Cameroon and Côte d'Ivoire contain some elements of transfer disclosure. Such transfers include transfers of revenues from the sale of state shares of oil and minerals, transfer of any revenue stream collected by the SOE on behalf of the state, income taxes and dividends. For more information refer to

- State owned enterprises

Proposal 9: Local content

It is proposed that implementing countries be encouraged to increase transparency around local content.

Background

Increasing transparency in local content would enable EITI stakeholders to access information related to company expenditure on suppliers and the procurement of goods and services. Multi-stakeholder groups would be encouraged to explore disclosure and reporting mechanisms similar to conventional EITI reporting. For more information refer to:

- Reporting in local content

Proposal 10: Midstream payments

It is proposed that implementing countries be encouraged to disclose midstream payments related to the transportation of oil, gas and minerals.

Background

EITI currently requires disclosure of upstream payments. Disclosure of midstream payments would enable users of EITI reports to access information on revenues from transportation of oil, gas and mining, including transit revenues in countries like Bulgaria and Ukraine which are currently considering EITI implementation. For more information refer to

- Midstream payments

Proposal 11: Social expenditures

It is proposed that the Board considers the following options:

i. **Disclosure of direct social expenditures becomes a minimum requirement;**

ii. **Disclosure of direct social expenditures is encouraged, but not required;**

Background

EITI Requirement #9-g encourages multi-stakeholder groups to develop reporting procedures for disclosure of social payments, where material. Several implementing countries disclose social payments, including Mongolia and Zambia. Where reconciliation is not possible, social payments are typically unilaterally disclosed by the companies.

Proposal 12: Data reliability

The Secretariat recommends that the EITI Rules are revised to require independent assurance that the EITI Report is comprehensive and reliable, allowing MSGs the flexibility to agree a procedure that builds on and takes into account existing national systems and capacities, and draws on international best practice.

Background

This proposal would be a modification of the current requirements 12 and 13 and draw on the work undertaken by the Chartered Institute of Public Finance and Accountability (CIPFA) in relation to the quality and reliability of data gathered for EITI reconciliations. CIPFA's concluded that:

- There is a substantial lack of clarity in the current set of EITI directives, [which] … impacts on the achievement of EITI requirements.
- There is considerable diversity of practice in the implementation of EITI in different countries. While some variation is necessary to reflect differences between countries,

the lack of clear distinction between different levels of assurance is unlikely to promote or encourage improvement.

- While allowing a degree of flexibility in the interpretation of the EITI directives is reasonable, this should reflect an understanding of the degree of independent assurance to be taken from the reconciliation process.

- Detailed drafting of specific EITI directives is needed. However, this can only be pursued when the EITI Board (or appropriate working group) concludes on what type of assurance is required by Criteria 2 and 3.

CIPFA recommends that the EITI should:

- Clarify inconsistencies and other lack of clarity in the EITI Criteria[3]

- Redraft EITI guidance to reflect the improved criteria, and to provide a consistent basis for assessing the achievement of compliance

- Develop a 'target' model[4] (for EITI assurance to inform assessment of partial achievement of independent assurance

- Encourage greater achievement of the target model through "country led" and "reconciler based" approaches[5]

The CIPFA paper provides additional detail regarding "country led" and "reconciler based" approaches. It also includes an alternative formulation for requirement 13.

CIPFA's recommendation for reformulating requirement 13

REQUIREMENT 13 The government is required to ensure that government reports are subject to adequate assurance procedures, and that any gaps in independent assurance are transparently disclosed.

1. It is required that Government acknowledges responsibility for the accuracy of the information in the EITI templates, which must be signed off by senior government officials or ministers.

2. It is recommended that the government assurance process relies as much as possible on existing procedures and institutions, and on international standards.

[3] CIPFA argues that "Criterion 2 on the audit of revenue and payments is difficult to understand. It can be interpreted as setting out an ideal set of requirements that might be very difficult for many countries to achieve. However, it can also be interpreted with a narrow scope that may sometimes provide little support to the EITI reconciliation". … "In addition, Criterion 3 on the EITI reconciliation process refers to international auditing standards in a confusing way. This is because the EITI reconciliation is not a type of engagement to which the body of international standards relating to audit applies (that is, when using the term 'audit' as defined within those international standards). This seems inconsistent and has caused confusion in practice. We suggest that it would be appropriate to reframe this criterion in terms of international standards on independent assurance" (CIPFA, 2012: 13)

[4] By 'target' model, CIPFA mean an 'ideal' EITI procedure that would achieve the desired outcome, i.e., independent assurance that the EITI data is reliable.

[5] See CIPFA pages 16-18

3. The requirement for government assurance will be fully satisfied, and no additional disclosures will be required if:

- Government EITI templates are audited by a Supreme Audit Institution or other independent auditor; AND
- Government accounts which include the EITI revenues in the template are audited by a Supreme Audit Institution or other independent auditor; AND
- Standards used for audit are based on INTOSAI International Standards for Supreme Audit Institutions (ISSAIs), or IAASB International Standards on Auditing (ISAs).

4. Disclosures in the reconciler's report will be required if

- Either Government EITI templates or relevant Government accounts are not audited; this might include circumstances where government audits focus only on compliance with budget law
- Assurance similar to independent audit is provided by parties who are not independent – this might include assurance by internal audit or from the work of inspectors or auditors who are not sufficiently independent to satisfy the independence requirements of ISSAIs 1 and 10.
- Standards used for audit or other assurance are not based on ISSAIs or ISAs. (It may however be possible to use local standards if these are of sufficient quality)

5. The disclosures at paragraph 4 above allow an assurance process to be used which is not in line with the full requirements at 3. However, they do not provide sufficient support for the situation where the only assurance provided is attestation by senior officials or ministers in line with paragraph 1 above – this can only be accepted if the target model of assurance is obtained for Requirement 12.

[the requirements could rank various levels of assurance achievement in line with other EITI scoring proposals, with attestation lowest, full audit highest]

6. The full range of disclosures outlined at 4 above will not be required if this requirement is augmented with assurance from Requirement 12, in line with the EITI target model for successful reconciliation. That is, Requirement 12 is fully satisfied in respect of all material company information, and the reconciler's report provides a clear statement that the reconciler is not aware of any evidence that the information provided for reconciliation is incomplete. Under these circumstances, the reconciler's report must disclose that the principal audit assurances for the reconciliation are provided through the audit of company information.

The International Secretariat suggests an approach that focuses on the desired outcome, i.e., independent assurance that EITI Reports are comprehensive and reliable. This would allow MSGs the flexibility to agree a procedure that builds on and takes into account existing national systems and capacities, and draws on international best practice. As suggested by CIPFA, additional guidance materials would be needed, including: (1) advising MSGs on how to assess the adequacy of existing systems; (2) providing guidance on models for EITI assurance. For more information refer to:

- EITI assurance data and quality review

Proposal 13: EITI Data standard

It is recommended that the Board:

1. Requires that implementing countries submit a core set of data from each published EITI report to the international Secretariat, which shall maintain an EITI Report database.

2. Encourages implementing countries to adopt the EITI Data Standard, and to make EITI data available in excel format.

Background

EITI Reports should be "publicly accessible, comprehensive and comprehensible". However, stakeholders have often found it difficult to access, interpret and utilise EITI data. The move toward publishing summary EITI reports is positive. However, in most cases EITI data cannot easily be related to the country's overall public finance statistics (e.g. it is difficult to determine the extractive industries' contribution to total government revenues), or to other data regarding the development of these sectors. It is also difficult to compare EITI data through time, and to compare data across countries. The Secretariat, in consultation with implementing countries and other stakeholders, is developing an EITI Data Standard that: (i) encompasses the core elements of EITI Reporting as set out in the EITI Rules; (ii) specifies a procedure for making EITI reports machine readable; and (iii) exploits opportunities to link EITI data to other relevant national and international information systems. For more information refer to:

- EITI Data Standard discussion paper

Proposal 14: Guidance to MSGs on EITI Workplans

It is proposed that the Working Group on Theory of Change develop more detailed guidelines that better reflect the MSG's wider aspirations with reference to requirement 5 on MSG workplans and requirement 21(c) on annual self-assessments.

Background

The Board established a working group to consider how to respond to the findings of the 2011 evaluation which suggested that the EITI needed a more detailed theory of change to support work planning, monitoring and evaluation of its results and impact.

The Working Group has developed the following recommendations for their further action:

1. With respect to Requirement 5, develop guidelines for MSGs on preparing workplans that include:

    a. overall objectives for the country and its different stakeholders concerning the impact and outcomes that they aim to achieve (through EITI implementation but including objectives beyond the EITI requirements);

    b. the activities that will lead to these outcomes; and,

    c. the measurable milestones and targets (indicators) that they will use to establish baselines, monitor and evaluate progress in achieving impact and outcomes;

    d. how this monitoring and evaluation might be combined with the self-assessment process proposed under requirement 21c (and potentially the strategic review). i.e. the workplan would provide the framework for the annual self-assessment report currently in requirement 21c. For example, some countries could therefore use this process to explain how they are allocating resource revenues and their strategies for achieving sustainability (as previously suggested by ICMM).

These guidelines may then form part of the World Bank's upcoming EITI Handbook and/or possible other guidelines or new rules that may emerge from the strategy discussions within EITI.

2. Develop a menu of possible indicators that countries might use to monitor and evaluate the outcomes and impact of these activities. This menu could serve as a reference guide to support MSGs in developing their own milestones and targets. Indicators would be drawn from country examples and best practice.

1.2 Revision of the EITI Requirements

The present 21 requirements are overlapping, repetitive, not necessarily sequential, and mix up process with outcomes. The Secretariat recommends a revision of the requirements so that they are presented more concisely and in a more outcomes-focused manner. For example, they might be distilled to the following six elements: the timeliness of the data, the comprehensiveness of the data, the reliability of the data, the explanation of discrepancies, the functioning of the MSG, and the communication and dissemination of the data (see box 1). The revised version could also encourage MSG to consider optional elements that can add value to the EITI process. This shift would improve the clarity of the requirements, the quality and consistency of the validation system, and the simplicity of communication.

Box 1 – Clarification of the EITI Requirements

The current 21 EITI requirements are not equal and divisible. Many are overlapping. Some are routine whilst others are complex. Some are process requirements, others are outcomes. The Secretariat proposes that the present 21 EITI requirements be distilled into possibly six simple elements that are outcome focused, easier to communicate, and easier to validate:

1. **Effective multi-stakeholder oversight and engagement** – requires a functioning MSG overseeing EITI implementation, including engagement with companies and full, independent, active, and effective participation of civil society (combining current requirements 1, 2, 3, 4, 6, 7, 10, 16 and 19).

2. **Regular and timely publication of EITI Reports** as per requirement 5e.

3. **Comprehensive data**. Requires coverage of all material revenue streams at all levels of government. Also addresses: (i) in-kind transfers/barter deals; (ii) social payments/transfers; (iii) whether all companies and government entities participated; (iv) the degree of disaggregation (combining current requirements 8, 9, 11, 14, and 15).

4. **Reliable Data** – Requires a credible reporting process to ensuring data reliability. (combining requirements 12 and 13).

5. **Identification of discrepancies**. That the report reflects a coherent methodology for identifying and address discrepancies (current

requirement 17).

6. **Communication.** Requires that the report is comprehensible and publicly assessable, and contributes to public debate (current requirement 18).

2. Redesigning the EITI's Validation system

2.1 Objectives

It is proposed that the Board considers proposals for revising the methodology for assessing EITI implementation performance which builds on the strengths of the current system and addresses its limitations. The Secretariat has proposed a a way to revise the existing system that draws on the earlier submission by the Secretariat ahead of the Board's meeting in October 2011, Board Paper 18-10[6], and the Proposal on Quality Assurance[7] (including Scoring) that was considered at the Strategy Working Group meeting in Henley.

This proposal has five overall objectives:

- to maintain the present concept of an EITI standard which must be met, whilst recognising and encouraging those countries that go beyond the standard.
- to put the focus of implementation on EITI Reports, rather than EITI validation, as it better reflects the EITI's ultimate product: annual, timely, comprehensive, reliable and comprehensible data.
- to put the focus of the standard and the assessment more on outcomes than on process.
- to better integrate the EITI into the governments' financial and other oversight systems.
- to strengthen the emphasis on country ownership.

The proposal also seeks to address the weaknesses with the current EITI Validation procedures, including the inherent temptation for validators to be generous when considering a country's compliance which puts a burden on the Board and Secretariat to reassess the assessments.

2.2 Summary of the modified quality assurance (validation)

The proposal is to replace the current validation arrangements with more nuanced quality assurance. It includes the following elements:

- A **self-assessment approved by the multi-stakeholder group**, containing two parts:
    a) one assessing performance against the EITI requirements; and

[6] http://eiti.org/files/Board%20Paper%2018-10%20Strategy%20Working%20Group_0.pdf

[7] http://eiti.org/files/SWG/Background%20Paper%20-%20Quality%20assurance%20including%20scoring.pdf

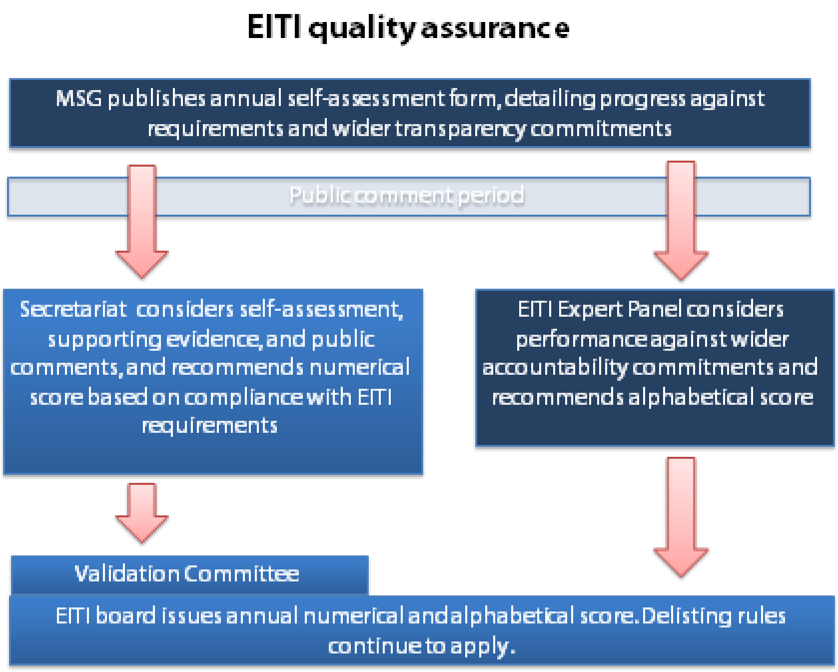
b) one assessing performance against wider transparency and accountability commitments agreed in the workplan.

- Based on the EITI requirements, the self-assessment of the performance against these, an **annual quality assurance, containing numerical scoring** for the EITI required outcomes, preserving the pass/fail compliance element.

- Based on the workplan and the self-assessment, an **annual alphabetical scoring** for wider accountability commitments that the MSG agreed to include in the workplan.

- The Board issues quality assurance, following recommendations of the numerical scoring by its Validation Committee and based on recommendations for the alphabetical scoring from an expert review panel. Numerical scores indicating that the requirements have been met, will lead the Board to conclude compliance.

- The current concepts of candidacy, compliance and delisting would remain.



2.3 Detail of the modified quality assurance (validation)

The following is detailed description of the proposed modified quality assurance arrangements.

Self-assessment

At a certain point each year – perhaps by the beginning of March – each country's MSG is asked to submit two papers:

1. an agreed workplan for the present year. The workplan should confirm to requirement 5a-c, with particular attention to the scope of the EITI report and dissemination activities. MSG are encouraged to set themselves stretching targets for which credit will be given in the alphabetical assessment.

2. an annual agreed self-assessment of the previous year's performance. This self-assessment is an elaboration of the annual progress reporting provision introduced in requirement 21c in 2011, though it would be required by all implementing countries, compliant and candidate. Particular emphasis should be given to the "actions to extend the detail and scope of EITI reporting or to increase engagement with stakeholders" (requirement 21c).

The self-assessment should contain two parts:

- one assessing performance against the EITI requirements; and
- one assessing performance against wider accountability commitments agreed in the workplan.

The MSGs should identify relevant innovations and linkages to the broader EITI Principles.

Any country failing to submit these documents by a given deadline can be considered for delisting unless the MSG can provide a clear and credible explanation.

The self-assessments reports would be published on www.eiti.org, inviting stakeholders to comment for a period of two months, before the Secretariat and Expert Panel issue their recommendations. This will increase transparency, and ensure everyone has an opportunity to comment on compliance and beyond compliance issues.

The numerical recommendation

During the open comment period, the International Secretariat will collate the self-assessment, any related comments, the previous year's reconciliation report, plus any other relevant documentation. If necessary, the Secretariat will consult with key stakeholders in country to help in making a recommendation of the country's numerical score.

The Secretariat's recommendation will be submitted to the Board's Validation Committee who will review the recommendation and make a proposal to the Board no later than six months after the receipt of the self-assessment.

Each one of the requirements would be numerically assessed, using the following scale:

0 No progress

1 Some progress toward meeting the requirement

2 Requirement met but not exceeded

3 MSG has implemented measures that exceed the requirements.

The final numerical score would then be an average of these scores.

If any of the requirements are not met, the total score can be no higher than 1 and the country will be assessed a not compliant, as with the present system. Countries not making any progress can be considered for delisting, as can countries which do not meet compliance within a 'maximum candidature period' without good reason, again as with the present system.

Compliant countries would have a score ranging between 2 and 3. The highest score possible would be 3.

These numerical scores should be considered as comparable amongst countries.

The alphabetical recommendation

The EITI Expert Panel will be established for the assessment of the performance against the wider accountability commitments made by the MSG in the workplan. It is foreseen that this would consist of three to five persons, a majority of which coming from implementing countries.

- Following the open comment period, the Expert Panel will receive the self-assessment from the MSG and any related comments (through the International Secretariat) and will review it against that year's workplan to assess to what extent the country has achieved progress against the wider commitments made (such as licensing, contracting, regulation, citizen participation, public oversight, revenue collection, revenue management, linking revenue spending to development planning, budget openness and public financial management, social and environmental issues, local content, etc.). The Panel may ask for further relevant documentation, the views of any stakeholders, and the assistance of the International Secretariat or experts. It may wish to visit the country. Just like the Secretariat in making it recommendations regarding the performance against the EITI requirements, the Panel will then make a recommendation to the Board no later than six months after the receipt of the self-assessment report. The alphabetical score would not be intended for comparison between countries. It would be based on how the MSG seeks to deliver to deliver on EITI's wider principles with some prompting questions eg. Is the EITI irreversible and sustainable? Are the scope of the reports being deepened and widened? Does the EITI link well with other governance reforms? Is the EITI helping to strengthen institutions? Is the EITI contributing effectively to public debate? Is the EITI helping affected communities?
- The scoring might be along the following lines:

  A The EITI is embedded in a coherent strategy for extractive industry transparency in line with the EITI principles.

  B Some steps have been taken to link the EITI to other measures to promote transparency and accountability.

  C No or limited steps have been taken beyond the EITI requirements

Guidance and good practice on these six outcomes would be adopted by the EITI Board.

The EITI Board would then issue a numerical and alphabetical score based on the recommendations from the Validation Committee and the Expert Panel.

2.4 Presentation of validation scores

Once the Board has agreed its scores for all countries the results would be published on the EITI website.

The final assessments should be simple to understand and to visualise. This might be done in a number of forms e.g. a table as below:

Country	EITI Score	
Azerbaijan	2.6	B
Burkina Faso	2.5	A
Chad	2.1	C
DRC	1.9	B
Ghana	1.8	B
Iraq	1.1	C

The timeline for scoring might look as follows for say, 2014:

Mar 2014: Country submits it self-assessment for 2013 including the numerical assessment for performance against the requirements, and the alphabetical assessment for performance against the contribution to the wider EITI principles against the 2013 workplan.

Mar-Apr 2014: Self-assessment of 2013 report on website with invitation for comments.

May-Jul 2014: International Secretariat assesses self-assessments and other documentation for all countries for numerical assessment by Validation Committee.

May-Sep 2014: Expert Panel assesses workplan and self-assessments and other documentation for recommendations on alphabetical assessments by Board for all countries.

Jul-Sep 2014: Validation Committee prepares recommendation on numerical assessments by Board for all countries.

Oct 2014: Board meets and agrees numerical and alphabetical scores for all countries for 2013. Table and grid published on EITI website, plus press release.

2.5 When to validate

The proposal is that all reporting countries are scored every year by the EITI Board, whether they are candidate or compliant. Currently, the Board can delist a country that does not produce its first report within 18 months of candidature. It is proposed that this element is retained.

In other words, once a country is admitted as a candidate, it would be informed when they would first be validate (i.e. they would be given enough time to produce their first report) and a deadline for achieving compliance (currently the “maximum candidature period”). For example, Solomon Islands admitted in, say, June 2012 would first be scored in 2014 based on the report they issued in 2013. They would have to achieve compliance in the scoring review of 2016 or be considered for delisting.

2.6 Suspension and delisting

As at present, the Board will have discretion to delist poor performing countries at key decision points eg. no production of first report within 18 months of becoming a candidate; no production of a report in a year; latest data is over two years old; a zero in numerical score on any of the individual requirements; and non-compliance within maximum candidature period. If a compliant country falls below the standard without good explanation, the Board can consider delisting.

2.7 Cost and work implications

Some have expressed concerns about the cost and work implications. The first thing to note when making an assessment of the costs and work implications is that <u>there would be no need for external validators in the current form</u>. Validation is costly, time-consuming and can undermine in-country ownership. Since the independence is often questioned, the Secretariat is usually forced to undertake follow-up reviews of draft validation reports and take on a de facto role of validator. The quality of the Validation reports varies significantly. A review undertaken by the Secretariat will ensure more consistent and equal assessment against the standard.

For the implementing countries, the suggested approach is likely to be lighter and cheaper than the present validation model, since all the elements are already part of their annual programme:

- Requirement 5e requires an annual reconciliation (no with data older than two years)
- Requirement 5a-c requires a workplan. Well organised MSGs are already writing these on an annual basis.
- Requirement 21c requires an annual self-assessment for compliant countries. The proposal here is that this be extended both in detail and form, as well as become a requirement for all implementing countries. It is hoped that this would not only be useful for Board assessment of performance, but also be a useful management and monitoring tool and help them establish their own outcome indicators and theory of change.

For the Board, Validation Committee, and International Secretariat, the process is unlikely to be heavier than the present given the demands that the present validation model already makes on them. The reports are already informally assessed in detail by the International Secretariat and any concerns are highlighted to the country and, where appropriate, to the Board. For the Validation Committee, although more countries will need to be assessed each year, each assessment will be considerably lighter than the validation process.

It is suggested that this proposal be piloted in a couple of countries to assess the resource implications for all stakeholders and to see if there might be areas for greater efficiency and linkage with other processes.

The Experts Panel would need to be established and would need support from the International Secretariat. This element of the proposal needs further consideration. However, having an Expert Review Panel assisting the Board of people drawn largely from implementing countries, would enhance legitimacy, increase peer lesson-learning, and ease some of the burden on the Board.

2.8 Conflicts of interest

Concerns have been expressed about having the International Secretariat both providing technical guidance to implementing countries and providing a first recommendation on numerical scoring to Validation Committee (and also advice as requested to the Expert Panel). Under the current arrangements, there are potential conflicts of interest, in that a number of validations have required the Secretariat to issue extensive and detailed complementary recommendations to the Board and with the current secretariat reviews.

Any potential conflict of interest can be mitigated by for example the International Secretariat separating its country advisory activities and the issuing of recommendations.

Decisions would as with the current arrangements be made by the Board.

2.9 Transition to new system

A transition to the new system would not be complicated. This system could be introduced to all countries at the same time e.g., from 2014.