Extractive Industries
Transparency Initiative

Understanding financial statements of state-owned enterprises

EITI Requirements 2.6, 4.2, 4.5 and 6.2

Guidance note

2019 EITI Standard

October 2021

This note has been issued by the EITI International Secretariat to provide guidance to implementing countries on meeting the requirements in the EITI Standard. Readers are advised to refer to the EITI Standard directly, and to contact the International Secretariat to seek further clarification.

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Introduction

Financial statements offer an overview of a company's financial performance and position over a given period. Companies, including state-owned enterprises (SOEs), typically prepare four main financial statements on a monthly, quarterly and annual basis: the balance sheet, income statement, cash flow statement and statement of shareholders' equity. These statements, along with relevant accounting policies and explanatory notes, provide a comprehensive view of a company's financial status.

In line with Requirement 2.6.b of the EITI Standard, SOEs must disclose their audited financial statements or key financial items where full statements are unavailable. This disclosure complements the financial requirements related to state participation and SOEs under the EITI Standard, including the disclosure of SOE financial relations with the state (Requirement 2.6), the sale of the state's share of production (Requirement 4.2), transactions related to SOEs (Requirement 4.5) and quasi-fiscal expenditures by SOEs (Requirement 6.2). These requirements ensure comprehensive transparency in SOEs' financial operations, promoting accountability in the extractive sector.

This note provides guidance to stakeholders, including EITI multi-stakeholder groups (MSGs), on locating information required by the EITI Standard within SOEs' standard financial statements.[1]

This diagram illustrates the financial relationships of an SOE with various parties, including the government, SOE subsidiaries, joint ventures and affiliates, extractive projects, lenders, shareholders and business partners.

KEY QUESTIONS ADDRESSED BY FINANCIAL STATEMENTS:

1. Is the company in a better financial position at the end of the reporting period than at the beginning of the year?
2. What resources does the company have?
3. How did the company use its cash during the reporting period?
4. What return on investment is the company achieving annually?
5. What financial risks does the company face?

Key concepts

The terms below outline the main elements of a consolidated financial statement. For a more detailed list of terms, see Annexe A.

Balance sheet

A balance sheet reports a company's assets, liabilities and shareholders' equity at a specific point in time, providing a basis for evaluating its capital structure and computing rates of return.

Income statement

An income statement, also called a profit and loss (P&L) statement, shows the company's income and expenditures, indicating whether it is generating a profit or loss for a given period. Along with the balance sheet and cash flow statement, it reflects a company's financial health.

Cash flow statement

A cash flow statement summarises cash inflows and outflows, measuring how effectively a company manages its cash position to meet debt obligations and fund operations.

Statement of shareholders' equity

A statement of shareholders' equity indicates changes in the value of shareholders' equity or ownership interest in a company over the accounting period, offering transparency about changes in equity accounts and business activities that affect shareholders' interests.

Financial audits

Financial audits provide an independent opinion of whether a company's financial statements present a "true and fair" view of its financial performance. In many countries, these audits are mandatory, assuring tax authorities and governments that companies accurately calculate their tax obligations. Audits also give investors confidence that the financial data is reliable for assessing investment risks.

Potential risks to SOE financial health

When reviewing SOE financial statements, MSGs should look out for the following red flags that may indicate financial health risks:

- **Rising debt-to-equity ratio**: An increasing debt-to-equity ratio may signal excessive debt. Debt of more than 50% of the company's capital structure is of concern, according to data providers like LexisNexis. It is recommended to also monitor the falling interest coverage ratio, which is calculated by dividing operating earnings by net interest payments. A value below five warrants further investigation, according to the Corporate Finance Institute (CFI).

- **Declining profit trends**: Three or more consecutive years of falling revenues raise concerns about the company's ability to provide returns on investment.

- **High "other" expenses**: Excessive expenses listed on balance sheets as "other" that are inconsistent or too small to quantify need scrutiny to understand their nature and likelihood of recurrence.

- **Unsteady cash flow**: Healthy organisations typically have fluctuating cash reserves. High cash stockpiles can indicate that accounts are being settled, and/or that there is not a large amount of new work, while cash shortages might indicate under-billing.

- **Rising accounts receivable or inventory**: Capital tied up in accounts receivable or unsold inventory can hinder investment returns. Significant bad debt provisions difficulties in recovering receivables, impacting cash flow.

- **Higher liabilities than assets**: While some companies experience cyclical asset and liabilities patterns, consistent liabilities exceeding assets may indicate over-leverage. In some cases, specific liabilities—such as unpaid cash calls or significant penalties and interest payable on delayed settlement of liabilities—could indicate internal challenges. Disclosures of contingent liabilities, such as unresolved legal issues, can signal potential future risks.

- **Declining gross profit margin**: The gross profit margin measures the ratio of profits to costs over a period. The profit margin must account not only for the costs to produce the product or service, but the additional funds required to cover operating expenses, such as cost of debt financing. A downward trend can indicate underlying financial challenges.

Other warning signs include consistently low profit margins, inadequate reinvestment, excessive short-term debt, diminishing returns and pending legal issues.

EITI Requirements related to state participation

EITI Requirement 2.6: State participation

The objective of EITI Requirement 2.6 is to ensure an effective mechanism for transparency and accountability for state-owned enterprises (SOEs), and state participation more broadly, through a public understanding of whether SOEs' management is undertaken in accordance with the relevant regulatory framework. This information provides the basis for continuous improvements in the SOE's contribution to the national economy whether financially, economically or socially, and strengthens understanding of the extent to which SOE investment decisions are aligned with long-term public interests.

This requirement covers:

- Publication of SOE audited financial statements
- Rules governing SOEs' financial relations with the state
- State and SOE ownership in the extractive industries
- State and SOE loans and guarantees
- SOE expenditures
- SOE procurement and sub-contracting
- SOE corporate governance and anti-corruption
- SOE investments and the energy transition S
- OE agents and intermediaries

EITI Requirement 4.2: Sale of the state's share of production or other revenues collected in kind

The objective of EITI Requirement 4.2 is to ensure transparency in the sale of oil, gas and/or mineral resources or other revenues collected in kind to allow the public to assess whether the sales values correspond to market values, and to ensure the traceability of the proceeds from the sale of those commodities to the national Treasury.

This requirement covers:

- In-kind revenues, proceeds of sales and transfers to the state
- Buyer selection process
- Sales agreements
- Disclosures by commodity buyers

EITI Requirement 4.5: Transactions related to SOEs

The objective of this EITI Requirement 4.5 is to ensure the traceability of payments and transfers involving state-owned enterprises (SOEs), as well as to strengthen public understanding of whether revenues accruable to the state are effectively transferred to the state and of the level of state financial support for SOEs.

This requirement covers:

- Company payments to SOEs
- SOE transfers to government
- Government transfers to SOEs

EITI Requirement 6.2: SOE quasi-fiscal expenditures

The objective of EITI Requirement 6.2 is to ensure that, where state-owned enterprises (SOEs) undertake extractive-funded expenditures on behalf of the government that are not reflected in the national budget, these are disclosed to ensure accountability in their management.

The requirement covers:

- SOE quasi-fiscal expenditures, including social services
- Public infrastructure
- Subsidies
- National debt servicing

Requirement 2.6: State participation

1. SOE audited financial statements

Audited financial statements of SOEs provide a comprehensive picture of their financial health, ensuring transparency and accountability in their operations.

EITI Requirement 2.6.b: SOEs in EITI implementing countries must publicly disclose their audited financial statements, or the main financial items (i.e. balance sheet, profit/loss statement, cash flows) where financial statements are not available. Legal and regulatory barriers inhibiting the timely disclosure of audited financial statements must be clearly documented by the reporting entity.

The main items in a company's financial statements include:

- **Balance sheet** as at the end of the period
- **Income statement** (also called "profit and loss statement") for the period
- **Cash flow statement** for the period
- **Statement of changes in equity** for the period
- **Notes** (narrative explanations) to the financial statements

Where to find information

When publicly disclosed, SOEs' financial statements are usually available on the SOE's website, the relevant government ministry's website, or on the corporate register. In some cases, SOEs' audited financial statements are attached to government audit reports published on the audit office's website. If it is not possible to publish the full audited financial statements, SOEs must document legal or regulatory barriers to publication.

Gaps with EITI disclosure requirements

Some SOEs only publish a summary of their consolidated financial statements, or omit the auditor's report. Some published financial statements may be outdated or unaudited.

How the EITI can add value

The EITI provides a platform for publishing financial statements, particularly where SOEs lack websites or face barriers. EITI countries could also play a role in collating financial statements and developing publicly accessible databases of audited financial statements in cases where none exist.

2. Rules and practices governing SOEs' financial relations with the state

The financial relationship between SOEs and the state includes transfers of funds, retained earnings, and reinvestments, which are governed by specific rules and practices.

2.1 Transfer of funds

SOEs regularly transfer funds to and from the state in the form of dividends, grants, subsidies, and budget allocations, governed by formal rules and practices.

EITI Requirement 2.6.a.i: Implementing countries must disclose an explanation of the role of SOEs in the sector and prevailing rules and practices regarding the financial relationship between SOEs and the state, including transfers of funds.

Where to find information

The rules governing the distribution of profits by SOEs, such as dividends or ad hoc transfers to government entities, are generally not described in the SOE's audited financial statements. Similarly, the rules on SOEs' entitlement to financial transfers from the government, such as budget transfers, subsidies or other financial assistance, are not typically found there.

These rules are usually codified in relevant laws, such as general SOE law, a law specific to a particular SOE, or the SOE's statutes or articles of incorporation (often called memorandum of incorporation). In some cases, these financial relations are formalised in the country's Public Finance Management Act.

Actual transfers from the government to the SOE are typically disclosed in the cash flow statement under "Financing Activities". They may be categorised as government "grants", "assistance" or "other income from the state".

SOE transfers to the government, including dividends, are generally reported in the SOE's balance sheet, under shareholder equity. Net profits transferred from the SOE to the state are often labelled as "distribution of profits" or shown as a deduction from retained earnings in the statement of stockholders' equity.

As government often holds interests in SOEs, the International Financial Reporting Standards (IFRS) (specifically IAS 24) require financial reports to include details on "related party" disclosures, transactions or amounts due/owed to the SOE. The materiality of these disclosures can provide insight into the SOE's performance in terms of financial transfers between the state and the SOE.

Gaps with EITI disclosure requirements

Not all SOEs or companies provide detailed components of operating income in their financial statements. Some report data under general "operational costs", which may include non-tax transfers to the government. Additionally, SOEs may not consistently report dividends; when this occurs, it is unclear if no dividends were paid or if they were categorised under other items.

There can also be differences in how SOE dividends are reported depending on the accounting method used. Accrual accounting reports dividends as they relate to profits from that year, while cash basis accounting records dividends when they are paid, which often related to profits from the previous year).

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of whether the financial transfers between the state and SOEs are in line with statutory procedures.
- Compare cash and accrual accounting of SOE transfers to the state, tracking decisions on dividends and their actual transfers to government, enhancing public oversight of SOEs' contributions to government revenues over time.
- Serve as a platform to analyse SOE payments to government, providing insights into the return on shareholder equity, which can inform public debate and policy on the management of oil, gas and mining SOEs.

EXAMPLES

GNPC (Ghana): According to Article 21 the 1983 GNPC Act (PNDCL 64), GNPC is required to make payments into the Consolidated Fund of any surpluses after taxes and contribution to its reserve fund.

Pemex (Mexico): In Pemex's 2014 consolidated financial statements (pp. 7 and 102), "Financing Activities" presents the value of financial transfers from the Mexican Federal Government to Pemex. These are categorised as "Increase in equity due to Mexican Government contributions" and are presented on an accrual accounting basis.

2.2 SOEs' retained earnings

SOEs retain earnings after dividend distribution, which can be reinvested in operations or saved for future use.

EITI Requirement 2.6.a.i: Implementing countries must disclose an explanation of the role of SOEs in the sector and prevailing rules and practices regarding the financial relationship between SOEs and the state, including retained earnings.

The term "retained earnings" refers to all profits retained after dividend distribution. These may be labelled as "retained earnings", "net earnings after dividends" or "appropriated/unappropriated retained earnings". Retained earnings can either be reinvested in company operations (including both operational and capital expenditures) or held in capital reserves or other accounts.

The formula to calculate retained earnings is: *Retained Earnings (RE) = Period Start RE + Net Income/Loss – Cash Dividends – Stock Dividends.*

Where to find information

The rules related to SOEs' ability to retain earnings are generally codified in relevant laws, such as a general SOE law, a law specific to a particular SOE, or in the SOE's statutes or memorandum of incorporation.

Information on SOEs' retained earnings are presented in the balance sheet under equity. Additional details are often provided in the notes to the financial statements.

Gaps with EITI disclosure requirements

Consolidated financial statements typically aggregate intra-group transactions, which means retained earnings for subsidiaries, joint ventures and affiliates in which the SOE holds an equity interests may not be disaggregated. However, the EITI requires public disclosure of retained earnings at a consolidated group level, as well as for any SOE subsidiaries considered material.

How the EITI can add value

EITI reporting can:

- Track trends in SOEs' retained earnings and analyse how they are managed and allocated, ensuring that distributions comply with legal frameworks and explaining any variances.

- Compare cash and accrual accounting of retained earnings, improving public understanding of SOEs' financial management over time.

EXAMPLES

GNPC (Ghana): Under Article 21 of the 1983 GNPC Act (PNDCL 64), GNPC is not permitted to retain earnings from its transfers of profits to the Consolidated Fund.

PT Pertamina (Indonesia): Note 26 of PT Pertamina's 2019 consolidated financial statements ("Retained earnings and interim dividend" and "Equity", pp. 3 and 107) disaggregates retained earnings into appropriated and unappropriated earnings for the financial years 2017 and 2018. This data is presented on an accrual basis.

2.3 SOE(s)' reinvestments

SOEs reinvest retained earnings into their own operations or their subsidiaries, affiliates, or joint ventures to support long-term growth and capital development.

EITI Requirement 2.6.a.i: Implementing countries must disclose explanation of the role of SOEs in the sector and prevailing rules and practices regarding the financial relationship between SOEs and the state, including reinvestment.

The term "reinvestment" refers to retained earnings for operating or capital expenditures within subsidiaries, affiliates, joint ventures or the parent group itself. This is distinct from retained earnings allocated to paid-up capital, capital reserves, bank accounts or other accounts.

Where to find information

Rules related to SOEs' ability to reinvest retained earnings are not usually detailed in the audited financial statements but are instead codified in relevant laws, such as a general SOE law, a law specific to a particular SOE, or in the SOE's statutes or memorandum of incorporation.

Information on reinvestments typically appears in the balance sheet under assets, and may also be found in the notes to financial statements, particularly sections on property, plant and equipment. The cash flow statement also reports capital expenditures under "cash flow from investing". The reinvestment rate is calculated by dividing capital expenditures by net income.

Gaps with EITI disclosure requirements

Consolidated financial statements reinvestment data at a group level, without disaggregating by subsidiary, joint venture and affiliate. IFRS 12 requires disclosure on interests in subsidiaries, joint ventures, joint arrangements, etc. At minimum, the EITI Standard requires disclosure of reinvestments at a consolidated level.

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of SOE reinvestments, focusing on return on investment.
- Compare cash and accrual accountings for SOEs' reinvestments, improving public understanding of financial management over time.
- Assess the alignment of SOE reinvestments with broader energy transition and climate risk considerations.

EXAMPLES

NNPC (Nigeria): Article 9 of the 1977 NNPC Act allows NNPC to reinvest retained earnings (or maintain a general reserve) after approval from the National Council of Ministers for the disposal of surplus funds.

GNPC (Ghana): Note 19, “Investments in subsidiaries”, in GNPC’s 2018 consolidated financial statements (pp. 49-52) provides the value of GNPC’s investment in its subsidiaries on an accrual basis.

2.4 SOE(s)’ third-party financing

Third-party financing is any funding for an SOE or its subsidiaries that comes from sources other than the SOEs’ shareholders or internal funds. This can include equity or debt financing from banks, institutional investors or retail investors. Equity financing involves raising capital by selling shares to retail or institutional investors, while debt financing entails borrowing funds to be repaid at a future date, usually with interest.

EITI Requirement 2.6.a.i: Implementing countries must disclose an explanation of the role of SOEs in the sector and prevailing rules and practices regarding the financial relationship between SOEs and the state, including third-party financing.

The term “third-party financing” refers to any type of equity or debt financing for the SOE’s operations (or those of its subsidiaries, affiliates and joint ventures) sourced from entities other than the SOE (including its subsidiaries, affiliates and joint ventures) or its shareholders.

Where to find information

Rules related to SOEs’ ability to raise third-party financing are generally codified in relevant laws, such as a general SOE law, a law specific to a particular SOE, or in the SOE’s statutes or memorandum of incorporation.

Information on third-party debt financing typically appears in the balance sheet under financial liabilities (current or non-current). The cash flow statement may provide details under “cash flow from financing activities”, with further information in the notes to the financial statements. Third-party debt financings are usually labelled as “short-term loan”, “long-term loan”, “line of credit”, “bond” or “Eurobond”.

Information on equity financing is usually disclosed in the balance sheet under “total liabilities and stockholders' equity” or “total liabilities and owner's equity”. The cash flow statement will reflect capital raised through equity issuance, although this does not affect the income statement.

Gaps with EITI disclosure requirements

Consolidated financial statements may present third-party debt financing in aggregate without breaking it down loan type. Similarly, while the value of equity issued during the review period is disclosed, the identity of the new equity holders may not be. At minimum, the EITI requires an aggregate disclosure of SOE third-party financing.

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of SOE third-party financing, analysing the reasons for and terms of both debt and equity financing.

- Compare cash and accrual accounting for third-party financing, improving public understanding of SOEs' financial management over time.

EXAMPLE

Pemex (Mexico): Article 106 of the 2014 Petróleos Mexicanos (Pemex) Law governs Pemex's ability to raise third-party financing (debt and equity). Debt limits for Pemex and its subsidiaries are set annually by Congress and published in the government's annual budget (Federal Income Law). These limits are detailed in Pemex's 2019 consolidated financial statement, Note 16 (p. 79).

Section 7.2 "Política de financiamiento y estado de la deuda documentada" of Pemex's 2019 annual report (pp. 88-93) presents information on its total debt, disaggregated by currency, interest rate, date of repayment/maturity and national and international debt holders. However, this data is not broken down by specific debt instrument.

2.5 SOE(s)' financial relations with subsidiaries and joint ventures

SOEs often hold interests in other entities, such as subsidiaries (where an SOE has a controlling share), joint ventures (a joint arrangement where two or more parties share control), or_associate companies/affiliates (entities in which the

SOE has a minority and non-controlling share).

EITI Requirement 2.6.a.i: Disclosures must include transfers, retained earnings, reinvestment and third-party financing related to SOE subsidiaries and joint ventures. This requirement aims to improve transparency of SOEs' direct and indirect interests. Key figures for each subsidiary and joint venture, including any transfers of funds between the parent company and its interests, should be provided.

The term "subsidiaries" refers to entities in which an SOE has a controlling share (i.e. 50% + 1 share). "Joint ventures" refers to joint arrangements where two or more parties have joint control and rights to the net assets of the arrangement.[2] "Associate companies" and "affiliates" refer to entities in which the SOE has a minority and non-controlling share.

Where to find information

Rules related to financial relations between SOEs and their subsidiaries and joint ventures are usually disclosed in the notes section of the SOE's consolidated financial statements, under the summary of significant accounting policies. This section typically outlines the accounting treatment for SOE investments in subsidiaries, joint ventures and associates/affiliates, as well as the SOE's entitlement to a share of profits from these entities.

Additional information may be found in the statutes of the SOE's subsidiaries, joint ventures and associates/affiliates, which often detail the financial relations between the SOE and its equity holdings.

The practices related to the financial relations between SOE and their subsidiaries and joint ventures are often only partially described in audited financial statements. Information on dividends collected by SOEs from subsidiaries, joint ventures and affiliates is usually included in the income statement under revenue and other income.

Further information on retained earnings, reinvestments and third-party financing of SOE subsidiaries, joint ventures and affiliates may also appear in the notes to the financial statements.

Gaps with EITI disclosure requirements

The notes to the financial statements typically describe the accounting treatment for different legal arrangement (e.g. subsidiary, joint venture, associate/affiliate) but do not always include a comprehensive list of companies in which the SOE holds equity, categorised by legal arrangement type.

The notes should confirm the legal arrangement type for each company where the SOE holds equity, although this information may not always be centralised in the audited financial statements. Information on interests in subsidiaries or joint ventures held for sale or any discontinued operations may also be lacking.

Consolidated financial statements often present income (i.e. dividends) from equity participations in subsidiaries, joint ventures and affiliates in aggregate, rather than by individual company. While the notes may sometimes break down dividend income by individual company, this is not always the case. The EITI requires disclosures by individual entity or source of income, which could also be included as part of "related party" transactions in the financial statement notes.

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of SOEs' financial relations with their subsidiaries and joint ventures, focusing on tracking transactions and revenues within the SOE group and at the consolidated group level.
- Offer a platform for analysing trends in dividends paid by subsidiaries and joint ventures to the SOE group, supporting public assessments of the SOE's return on investments over time.

EXAMPLES

GNPC (Ghana): Note 3.4, "Interests in joint arrangements" to GNPC's 2018 consolidated financial statements (pp. 19-20) describes the accounting policies for GNPC's interests in joint operations, joint ventures and associates. This aligns with International Financial Reporting Standards (IFRS 11) and International Accounting Standards (IAS) 39.

KazMunayGas (Kazakhstan): Note 7 "Share in profit of joint-ventures and associates, net" in KazMunayGas's 2019 consolidated financial statements (p. 27 of notes) shows net profits received from equity interests in joint ventures and affiliates. Note 19, "Investment in joint-ventures and associates" (pp. 52-61) provides summarised financial information on assets, liabilities, equity, revenues and profit for each joint venture and affiliate where the SOE holds equity. These figures are presented on an accrual basis.

3. State and SOE ownership in the extractive industries

Ownership refers to the rights and responsibilities of individuals holding a legal or equitable interest in a company. Ownership information helps stakeholders evaluate the nature of, and risks associated with, a company's interests in subsidiaries, joint ventures, associates or unconsolidated entities, and the impact of these interests on its financial position.

EITI Requirement 2.6.a.ii: Implementing countries must disclose the level of government and SOE ownership in oil, gas and mining companies operating within the country's oil, gas and mining sector, including ownership held by SOE subsidiaries and joint ventures, as well as any changes in the level of ownership during the reporting period.

Where to find information

Consolidated financial statements typically show the aggregate value of a company's investments in joint ventures and affiliates in the balance sheet under "assets". Impairments related to these investments are shown under "costs and expenses" in the income statement. A list of subsidiaries, joint ventures and affiliates may be included in the notes, though it is not always comprehensive. In some cases, this information can be found in the supplementary section of the annual report.

Consolidated financial statements often do not provide a comprehensive list of equity interests held by an SOE's subsidiaries, joint ventures or affiliates. While they usually include direct equity interests held by SOEs, they may not cover indirect equity interests held by companies in which the SOEs own shares.

The notes to the consolidated financial statements usually disclose:

- The terms attached to government and SOE ownership, i.e. the treatment of assets and liabilities related to equity holdings (typically in the section on accounting policies);
- Changes in government and SOE ownership in subsidiaries, joint ventures and affiliates;
- The terms of changes in SOE ownership in subsidiaries, joint ventures and affiliates.

Gaps with EITI disclosure requirements

Consolidated financial statements often include a list of major subsidiaries, joint ventures and affiliates, but equity interests in smaller companies are usually presented in aggregate under a single category labelled "Other".

- **Terms of ownership:** Consolidated financial statements often provide the terms attached to SOE equity interests by company type (e.g. subsidiary, joint venture, affiliate), but not consistently cover individual companies.

- **Changes in ownership:** Information on changes in equity ownership typically covers direct equity participations, not changes in ownership held by SOE subsidiaries, joint ventures or affiliates. Indirect interests, e.g. interests of subsidiaries or associates/affiliates, are usually excluded. For tax authorities that are handling capital gains tax issues on transfer of ownership, challenges can emerge where these disclosures are made at a parent company level and not disclosed at the subsidiary level.

How the EITI can add value

EITI reporting can:

- Provide and assessment of changes in state and SOE ownership of oil, gas and mining companies and their participation in extractive projects over time.
- Improve transparency around SOE restructuring, especially during wide-ranging restructurings implemented over several years.
- Clarify the responsibilities of the state and SOEs in covering costs associated with SOE subsidiaries, joint ventures and affiliates over the course of the business cycle.

EXAMPLES

- **Naftogaz (Ukraine):** Note 1, "The organisation and its operations", in Naftogaz's consolidated financial statement for 2019 (p. 13) provides an overview of its principal subsidiaries and joint operations, though the type of equity interest is not stated. Note 6, "Investments in associates and joint ventures", (pp. 25-26) covers interests in affiliates/associates and other joint ventures, without specific terms for equity stakes. Note 7, "Other non-current assets", highlights expenses related to a soil exploration and development concession with another company, including its losses related to production sharing agreements.
- **Kumul Mineral Holdings Ltd (KMHL) (Papua New Guinea):** Note 21, "Equity", in KMHL's 2020 consolidated financial statements (p. 96), describes the sale of its equity interest in Eda Oil Ltd to MOL, including the equity valuation and consideration paid.
- **Equinor (Norway):** Note 4, "Acquisitions and disposals", in Equinor's 2019 consolidated financial statements (pp.175-177) details acquisitions and disposals of equity interests in companies and participating interests in oil and gas projects, including transaction values and financial consideration paid or received.

4. State and SOE loans and guarantees

SOEs and the state may provide or receive loans and guarantees to or from extractive companies, which can influence financial stability and project outcomes.

EITI Requirement 2.6.a.ii: Implementing countries must disclose details of government and SOE loans or loan guarantees to oil, gas and mining companies, including loan tenor and terms. Multi-stakeholder groups are encouraged to consider comparing loans terms with commercial lending terms.

The term "loan tenor" refers to the duration of the loan or debt instrument, while "loan terms" refers to the repayment schedule and the interest rate.

Where to find information

Information on third-party debt financing for SOEs is usually found in the balance sheet under financial liabilities (current and non-current). Related party transactions, which include loans between the government and SOEs, may also be covered in the notes.

- **Government loans:** The notes typically describe loans or loan guarantees received from the government in aggregate. Government loans and guarantees provided to specific companies are often detailed in the government's budget execution report or publications by the Ministry of Finance.

- **SOE loans:** Loans from an SOE to its subsidiaries are usually recorded in the financial statements of the subsidiaries but may not appear in the consolidated financial statements of the SOE group. However, company loans to joint ventures and affiliates are usually recorded in the consolidated financial statements in the cash flow statement under "cash flow from investing activities". The terms of these loans may be described in the notes to the financial statements.

Gaps with EITI disclosure requirements

- **Government loans:** Financial statements typically describe loans and guarantees provided by the government in aggregate, and not broken down by individual loans or guarantee. Specific details such as the loan tenor, repayment modalities or interest rate are often lacking.

- **SOE loans:** Financial statements do not always list loans provided by an SOE to its subsidiaries. Information on loans to joint ventures and affiliates may lack details on the loan tenor, repayment modalities and interest rate.

How the EITI can add value

- EITI reporting can establish a framework for SOEs to disclose comprehensive details of their loans and guarantees, which is a key part of their accountability to the state and the public.
- Clear and consistent disclosures on contingent liabilities such as loans and guarantees help address fiscal transparency concerns.

EXAMPLE

Naftogaz (Ukraine): Note 4, "Balances and transactions with related parties", in Naftogaz's 2019 consolidated financial statements (p. 23) presents the aggregate value of government (sovereign) guarantees provided to Naftogaz at the end of 2018 and the end of 2019. The notes to the consolidated statement of financial position (p. 7) and Note 12, "Borrowings and Other Non-Current Liabilities" (pp. 32-33), provide additional information on government guarantees, though only the aggregate value of borrowings guaranteed by the state is disclosed, without specifying the precise third-party financial arrangements covered by these guarantees.

5. SOE expenditures

SOEs' expenditures are divided into operational costs for day-to-day activities and capital investments for long-term asset development and growth. "Operating expenditures" refer to the recurring costs incurred by an SOE in its day-to-day operations, typically arising from the sale of oil, gas and products in a given year. These include:

- General, operating, selling, administrative and marketing costs
- Employee and facility expenses (e.g. rent)
- Exploration expenses if not capitalised (i.e. if the sources of funding for an expense are not clearly defined)
- Depreciation, impairment and amortisation (if related to operations)
- Costs of purchasing oil, gas and petroleum products

Operating expenditures exclude tax or non-tax transfers to the state and financial costs, such as interest and other borrowing-related charges.

"Capital expenditures" refer to the cash spent by an SOE on acquiring or upgrading physical assets in a given year. This includes investments through the acquisition or leasing of property, equipment (wells, plants, etc.), or costs related to upgrading and maintaining existing assets to extend their life. Capital expenditures only cover acquisition costs that are capitalised. Exploration costs, such as drilling exploratory wells, are included only if explicitly capitalised. These expenditures reflect the SOE's investments aimed at future growth.

EITI Requirement 2.6.c: Implementing countries must describe the rules and practices governing SOEs' operating and capital expenditures.

Where to find information

- **Operating expenditures:** Rules related to SOEs' operating expenditures are generally codified in laws (e.g. general SOE laws, SOE-specific laws) or in the SOE's statutes or memorandum of incorporation.

- **Capital expenditures:** The regulatory framework for capital expenditures is also codified in relevant laws of statues, and the accounting policies in the financial statements provide information on asset depreciation and amortisation. Details on actual capital expenditures are typically disclosed as assets in the balance sheet and in the cash flow statement under "investing activities".

Gaps with EITI disclosure requirement

The way in which SOEs report their expenditures varies significantly across jurisdictions. It is often challenging to distinguish between operational and capital expenditures in financial statements. It may also be difficult to identify whether a cost has been capitalised, based on the available data.

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of whether SOEs' operating and capital expenditures comply with relevant rules and regulations.

- Offer a platform for evaluating trends in SOE's capital expenditures over time, situating these expenditures within the broader context of the SOE's financial performance and future growth prospects.

EXAMPLES

GNPC (Ghana): Note 15, "Petroleum projects", of GNPC's 2018 consolidated financial statements (p. 47) detail operating expenditures for oil and gas projects, broken down by project.

Equinor (Norway): Equinor's 2019 consolidated financial statements present net capital expenditure and investment in the consolidated cash flow statement (p. 157). Information on capital expenditure is detailed in the notes on "Property, plant and equipment" (p. 188) and in Note 4 "Acquisitions and disposals". Equinor's annual report provides some information on the rules related to capital expenditure.

6. SOE procurement and sub-contracting

SOEs procure goods and services from external sources and may subcontract parts of their operations. These processes should be governed by rules ensuring transparency and fair competition.

EITI Requirement 2.6.c: Implementing countries must describe the rules and practices related to SOEs' procurement and sub-contracting. The term "procurement" refers to the acquisition of goods, services or works from an outside external source.

Where to find information

Consolidated financial statements typically do not provide information on SOEs' procurement and sub-contracting rules or practices. However, some SOEs disclose this information on their corporate websites.

Procurements may also be governed by the general procurement legal framework of the respective state. In instances where an SOE has undergone a performance audit, the performance audit report may review the SOE's procurement rules and practices.

Gaps with EITI disclosure requirements

Some SOEs disclose procurement and sub-contracting rules on their websites, but this information often focuses on legal and regulatory procedures, rather than providing an overview of actual procurement and sub-contracting practices.

How the EITI can add value

EITI reporting can:

- Provide an annual assessment of how well SOEs' procurement and sub-contracting practices align with relevant rules and regulations.
- Offer a platform for evaluating the robustness of procurement and sub-contracting policies and practices, reducing the risk of mismanagement or undue discretion in the awarding of contracts.
- Help align SOEs' contracting disclosures with international standards, such as the Open Contracting Data Standard (OCDS), which fosters greater transparency and accountability.

EXAMPLE

Pemex (Mexico): While Pemex's consolidated financial statements do not describe procurement or sub-contracting rules and practices, the company's website includes a section on "Suppliers", which details procurement rules and procedures, while the section on "Contracting procedures" provides information on contracting procedures. The website also includes access to the "Public information system suppliers and contractors", and the company launched a webpage with information on all its procurement and supplier contracts, updated on a monthly basis.

7. SOE corporate governance and anti-corruption

Corporate governance in SOEs includes the rules and practices for appointing Boards, defining mandates, establishing codes of conduct and implementing anti-corruption measures to ensure accountability and transparency.

EITI Requirement 2.6.c: Implementing countries must describe the rules and practices related to SOEs' corporate governance, e.g. composition and appointment of the Board of Directors, Board's mandate and code of conduct.

Expectations for EITI supporting companies: SOEs that are EITI supporting companies are expected to publish their anti-corruption policies and are encouraged to engage in rigorous due diligence processes (Expectation 7).

Where to find information

While consolidated financial statements often include information on the composition of the SOE's Board of Directors, they typically do not provide details on the Board's appointment process, mandate, code of conduct, or the company's anti-corruption or due diligence practices. However, some SOEs disclose such information on their corporate websites.

If SOEs are governed by a general or specific SOE law, the appointment process and/or mandate may be outlined in the relevant legislation.

Gaps with EITI disclosure requirements

- **Board appointment:** Descriptions on SOE websites often focus on statutory appointment rules rather than the actual practices.
- **Board mandate:** Information about the mandate of the Board of Directors, when disclosed on corporate websites, is often brief and lacks details.
- **Code of conduct:** SOEs do not always publish full version of their code of conduct on their websites.
- **Anti-corruption and due diligence policies:** The level of detail in published anti-corruption policies and due diligence procedures varies across SOEs. The level of detail provided can impact the public's understanding of the robustness of these policies.

How the EITI can add value:

EITI reporting can:

- Clarify governance structures and provide more context on SOEs' corporate governance, including how Boards of Directors are appointed in practice, their mandate and the overall governance framework.
- Offer a platform for clarifying SOEs' decision-making and accountability processes.
- Help align SOEs' corporate governance practices with international standards, such as the OECD Guidelines on Corporate Governance of State-Owned Enterprises, which offer recommendations for strengthening SOE governance to improve competitiveness, efficiency and transparency.

EXAMPLE

Naftogaz (Ukraine): While Naftogaz's consolidated financial statements do not cover corporate governance rules, its website provides information on corporate governance, including Board composition and reforms, in line with G20/OECD Principles of Corporate Governance.

8. SOE investments and the energy transition

SOE investments in the extractive industries can have a significant impact on a country's energy transition and climate policies and may support or impede efforts to manage climate-related risks.

EITI Requirement 2.6.d: Where applicable, SOEs are encouraged to disclose investments in the extractive industries (including assets and liabilities) and how their investment decisions are aligned with energy transition and climate risk considerations.

Where to find information

Consolidated financial statements consistently provide information on the company's investments. Capital expenditures are typically reported under the "cash flow from investing" section of the cash flow statement in the balance sheet. The notes related to "tangible fixed assets" often disclose SOE investments in exploration and production, including both development and dismantling costs.

Gaps with EITI disclosure requirements

Consolidated financial statements typically do not provide an overview of the SOE's investment plans beyond the period under review, nor do they describe how investments align with energy transition and climate risk considerations. However, they often contain some forward-looking commentary, though this is not always directly linked to the company's broader investment strategy or assumptions about the future.

How the EITI can add value:

EITI reporting can:

- Provide additional context on SOEs' investment plans, particularly in relation to energy transition and climate risk considerations.
- Clarify the impact of energy transition and climate risk on SOEs' investment strategies.
- Help align SOEs' investment planning with the country's broader energy transition and climate risk considerations.

EXAMPLE

Ecopetrol (Colombia): The National Oil Company of Colombia, Ecopetrol, has been subject to new green taxonomy as well as environmental, social and governance (ESG) and climate risk reporting requirements for publicly listed companies since 2022. Ecopetrol's website discloses the SOE's reports in line with guidance from the Task Force on Climate-Related Financial Disclosures (TCFD), Climate Disclosure Project (CDP) and the Sustainability Accounting Standards Board's (SASB) Metrics Report.

9. SOE agents and intermediaries

SOEs frequently engage with agents, intermediaries, suppliers or contractors to facilitate their operations. Transparency around these relationships can help to identify potential conflicts of interest and ensure accountability.

EITI Requirement 2.6.e: Where feasible, SOEs are encouraged to disclose the identity and beneficial ownership of their agents or intermediaries, suppliers or contractors for material transactions.

Where to find information

Consolidated financial statements typically do not provide detailed information on a company's agents, intermediaries, suppliers or contractors. However, some SOEs disclose such information on their corporate websites as part of efforts to enhance transparency in procurement practices.

Gaps with EITI disclosure requirements

SOEs' disclosures regarding their agents, intermediaries, suppliers and contractors tend to be limited to the names of these entities, with little additional detail. Few SOEs publish beneficial ownership information of their agents, intermediaries, suppliers or contractors.

How the EITI can add value:

EITI reporting can:

- Support SOEs in establishing robust record-keeping and disclosure practices concerning the identity of their agents, intermediaries, suppliers and contractors.

- Clarify the beneficial ownership of SOEs' key agents, intermediaries, suppliers and contractors.

- Serve as a platform for discussing and assessing any risks related to the identity and roles of SOEs' agents, intermediaries, suppliers and contractors.

EXAMPLE

Pemex (Mexico): The National Oil Company of Mexico, Pemex, discloses information on all procurement and supplier contracts concluded by its upstream subsidiary, Pemex E&P, on a monthly basis. This includes an updated public registry of the names of Pemex's suppliers and contractors, along with a monthly report of payments to them. However, the beneficial ownership of Pemex's suppliers and contractors is not disclosed.

Requirement 4.2: Sale of the state's share of production or other revenues collected in kind

In many resource-rich countries, governments and SOEs receive fiscal payments from companies in-kind through physical transfers of oil, gas or minerals, rather than monetary payments, which are then sold to generate revenue.

1. In-kind revenues, proceeds of sales and transfers to the state

Governments or SOEs collect in-kind revenues from production, sell these commodities, and transfer the proceeds to the state treasury or other designated entities.

EITI Requirement 4.2.a: Where the sale of the state's share of production of oil, gas and/or mineral resources or other in-kind revenues is material, the government, including SOEs, must disclose the **volumes received and sold**, the **revenues from sales**, and the **revenues transferred to the state** from the sales. Data must be disaggregated by buying company and to levels commensurate with the reporting of other payments and revenue streams.

In-kind revenues include:

- **Production sharing agreements (PSAs):** The government or SOE receives a share of profit oil or gas as a fiscal payment.
- **Service contract production:** Governments pay companies with physical commodities in exchange for extracting resources.
- **In-kind tax or royalty payments:** Companies may meet tax and royalty obligations with commodities instead of cash.

Shares of production collected by SOEs that are not considered in-kind revenues on behalf of the state include production from fields or mines fully or partially owned by the SOE, where the SOE operates and retains its share of production. In joint ventures, SOEs may receive equity commodities based on their ownership stake, with this share often reduced by the operator's costs. Additionally, when the SOE holds equity in PSAs, they may receive cost and profit commodities (e.g. "cost oil" or "profit oil"), which are separate from the state's share managed by the SOE.

Where to find information

- **Volumes of state in-kind revenues collected:** Consolidated financial statements typically provide information on the SOE's share of production but rarely include details on in-kind revenues collected for the state. Some SOEs maintain separate accounts of operations for the state and their own commercial activities, with distinct financial statements.
- **Volumes of state in-kind revenues sold:** Consolidated financial statements often report crude oil sales volumes, but seldom distinguish sales conducted

on behalf of the state. However, some SOEs maintain separate accounts, and some may disclosure their commodity sales on their corporate websites.

- **Value of proceeds of sales of state in-kind revenues:** Consolidated financial statements typically include proceeds from commodity sales under “Revenue” in the income statement, but do not clearly separate revenues from sales made on behalf of the government, nor do they break this down by buyer. Some SOEs maintain separate accounts, and best practices include publishing more detailed information on crude oil sales on corporate websites.

- **Value of transfers to the state of proceeds of sales of state in-kind revenues:** Consolidated financial statements do not typically present information on transfers of in-kind revenue sales to the state Treasury. Instead, these details are usually found in government reports, such as in annexes to budget execution reports published by the Ministry of Finance.

Gaps with EITI disclosure requirements

- **Volumes of state in-kind revenues collected:** In-kind revenues are generally presented in aggregate, not broken down by project, as required by the EITI Standard. Some SOEs only publish summaries of their consolidated financial statements, lacking the required detail.

- **Volumes of state in-kind revenues sold:** As with collected revenues, SOEs' financial statements often present sales volumes in aggregate, rather than disaggregated by project or buyer. Corporate websites can provide more detailed data, but this practice is not yet widespread.

- **Value of proceeds of sales of state in-kind revenues:** Financial statements and annual reports typically do not break down the proceeds of sales of the state's in-kind revenues by buyer. However, where SOEs publish information on crude oil sales on corporate websites, this may include sales data disaggregated by buyer and cargo.

- **Value of transfers to the state of proceeds of sales of state in-kind revenues:** While financial statements present the value of payments to the state of taxes and dividends, they generally do not include details on the transfer of sales proceeds to the state. Payments may be lumped into operational expenditures, without being disaggregated.

How the EITI can add value

EITI reporting can:

- Enable SOEs to demonstrate the efficiency of the commercialisation process for the commodities they produce.

- Provide a platform for annual assessments of the terms of trade for the state's commodity sales, allowing for multi-year and cross-country comparisons of commodity sales prices and terms.

EXAMPLE

GNPC (Ghana): While GNPC's 2018 consolidated financial statements do not provide detailed information on volumes of crude oil sold on behalf of the state, it provides information on all crude oil liftings, sales and proceeds on its website, disaggregated by buyer and cargo, under "Crude Oil Sales Reports" in open data format.

2. Buyer selection process

Commodity sales by SOEs often involve selecting buyers based on various criteria. Transparency in this process helps ensure accountability and fairness.

EITI Requirement 4.2.b: Implementing countries, including SOEs, are encouraged to disclose a description of the process for selecting the buying companies; the technical and financial criteria used to make the selection; the list of selected buying companies (including beneficial ownership information where available, the identity of intermediaries or agents where applicable, and any material deviations from the applicable legal and regulatory framework governing the selection of buying companies), and the related sales agreements.

Where to find information

- **Rules for selecting buyers:** Neither consolidated financial statements nor their annual reports typically describe the statutory process for selecting buyers of commodity sales. However, this information may sometimes be found on the SOE's website.

- **Buyer selection practices:** Consolidated financial statements and annual reports do not usually disclose information on the practice of selecting buyers and the identity of the buyers. In some cases, this information is published on the SOE's website.

- **Identity of intermediaries and agents:** Consolidated financial statements and annual reports do not usually disclose information on the identity of SOEs' intermediaries and agents. Some national oil companies may publish payments made to intermediaries and agents in their financial statements.

Gaps with EITI disclosure requirements

- **Buyer selection rules and practices:** Information on the statutory rules for selecting buying companies is often not published on SOE websites. While some SOEs may disclose this information on their corporate websites, they usually do not include an overview of actual practice, or deviations from the rules.
- **Buyer identity and beneficial ownership:** While many SOEs disclose cargo-level oil sales data that identifies buyers, legal no beneficial ownership information is rarely included. Some SOEs note that beneficial ownership could be requested but has not been provided, despite most national oil companies reporting due diligence buyer ownership.

How the EITI can add value

EITI reporting can:

- Enhance transparency in the buyer selection process by requiring the disclosure of selection criteria used, buyer identities and beneficial ownership.
- Provide a platform for identifying any deviations from legal frameworks governing buyer selection, ensuring that SOEs comply with statutory rules.
- Encourage SOEs to disclose information on intermediaries and agents involved in commodity sales, including any fees or commissions paid.

EXAMPLES

- **NNPC (Nigeria):** NNPC Trading Ltd's website provides an overview of the crude oil buyer registration process, including required documents and buyer registration process.
- **Pemex (Mexico):** Pemex's trading subsidiary, PMI Comercio Internacional, maintains a dedicated website with information on general terms and conditions, pricing and commercial guidelines.
- **Sonangol (Angola):** Sonangol publishes the aggregate value of its payments on commissions and fees to intermediaries in Note 30 (p.92) of its 2021 consolidated financial statements.

3. Sales agreements related to the state's in-kind revenues

Sales agreements outline the terms and conditions under which the state or its SOEs sell in-kind revenues to buyers. Publishing such agreements can ensure transparency and accountability in commodity sales.

EITI Requirement 4.2.c: Implementing countries are encouraged to disclose the related sales agreements with buying companies.

Where to find information

Commodity sales contract templates are sometimes published on SOEs' websites. However, final versions of these agreements are rarely made public. Publicly listed companies may disclose some contracts as part of their reporting requirements.

Gaps with EITI disclosure requirements

SOEs generally do not publish final commodity sales agreements. However, national EITI processes are leading to the publication of model commodity sales agreement templates, such as in Iraq, Mexico and the Republic of the Congo. Publicly listed companies are sometimes required to disclose commodity sales agreements involving state partners, as in the case of the LNG sales contract with BP and Kosmos Energy in Mauritania and Senegal.

How the EITI can add value

EITI reporting can:

- Improve public oversight of state commodity sales and their contractual basis, ensuring that transactions are conducted fairly and in line with market practices.
- Enable stakeholders to assess whether the state receives a fair value from its in-kind revenues in line with the terms of the sales agreement(s).
- Provide a platform for comparing the terms of state commodity sales across countries, fostering best practices and reducing the risk of mismanagement or corruption in sales processes.

EXAMPLES

SOMO (Iraq): The crude oil sales contract template was published in Appendix 6 of Iraq's 2012 EITI Report (pp. 170-190), although it is not available on the SOMO or Ministry of Oil website.

National Hydrocarbons Commission (Mexico): The oil and gas regulator CNH publishes the annual crude oil marketing contract for the sale of the government's in-kind oil revenues on its website, though contracts between the marketer and buyers are not publicly disclosed.

SMH and PETROSEN (Mauritania and Senegal): The Sales Purchase Agreement for liquefied natural gas (LNG) from the Greater Tortue/Ahmeyim gas project was published on the United States Securities and Exchange Commission (SEC) portal, as required for publicly-listed companies in the US.

4. Commodity buyer disclosures

Commodity buyers, which include trading companies and refiners, can play a key role in ensuring transparency around purchases of the state's resources, helping to enhance accountability in commodity trading.

EITI Requirement 4.2.d: Companies buying oil, gas and/or mineral resources from the state or SOEs are encouraged to disclose volumes received and payments made for such purchases. This could include payments (in cash or in kind) related to swap agreements and resource-backed loans.

Companies are encouraged to publish data disaggregated by individual seller, contract or sale. The disclosures could for each sale include information on the nature of the contract (e.g. spot or term) and load port.

Where to find information

Consolidated financial statements typically do not disclose a company's specific purchases from SOEs. However, a growing number of buyers are publishing this information through annual payments to government reports.

Gaps with EITI disclosure requirements

While some buyers disclose their purchases, these do not consistently meet the EITI Standard's requirements. They often fail to disaggregate purchased volumes and values by individual cargo, and do not usually differentiate between state's in-kind revenues and the SOE's own equity commodity sales.

How the EITI can add value

EITI reporting can:

- Promote a level playing field by enhancing transparency in the buyer selection and sales process.
- Improve transparency on the ownership of contractors and help clarify the relationship between the SOE and its business partners, reducing counterparty risk and strengthening the SOE's credibility with lenders and investors.
- Align buyer selection practices with international standards such as the OECD's guidance for SOEs on "How to Select Buyers of Oil, Gas and Minerals", supporting transparent and competitive sales processes.

EXAMPLES

- **Commodity traders:** Commodity traders Gunvor and Trafigura and have published annual payments to government reports related to its purchases of crude oil from EITI countries on their websites since 2016, sometimes disclosing data not yet available from the SOEs themselves.
- **TotalEnergies:** TotalEnergies publishes its payments for the purchase of oil and gas from national oil companies alongside its payments to government related to exploration and production, in annual reports available on its website.

Requirement 4.5: Transactions related to SOEs

EITI Requirement 4.5: EITI multi-stakeholder groups must ensure that the reporting process fully addresses the role of SOEs. This includes comprehensive and reliable disclosures of material company payments made to SOEs, SOE transfers to government agencies and government transfers to SOEs.

The term "company payments to SOEs" refers to revenue collection by SOEs on behalf of the state, whether through fiscal instruments (e.g. royalties) or ownership (e.g. dividends).

1. Company payments to SOEs

Where to find information

Consolidated financial statements present the value of dividends received from subsidiaries, joint ventures and affiliates in the "revenue" section of the income statement.

Gaps with EITI disclosure requirements

Information on dividends from subsidiaries, joint ventures and affiliates is not always broken down by individual company.

EXAMPLE

GNPC (Ghana): GNPC's 2018 consolidated financial statements (pp. 8 and 13) and Note 20 "Investment in associates and joint-ventures" (pp. 54-55) provide the value of dividends received from all subsidiaries, joint ventures and other affiliate companies. The financial statements present the aggregate value of revenues from oil and gas operators as contributions to the training and technology fund, though not disaggregated by company. These figures are presented on an accrual basis.

2. SOE transfers to the government

Where to find information

Information on SOE transfers to the government, such dividends, are typically presented in the SOE's balance sheet under "shareholder equity". Transfers of net profits from the SOE to the state are often labelled as "distribution of profits" or "statement of stockholders' equity as a subtraction from retained earnings", among other labels.

Gaps with EITI disclosure requirements

Not all companies record the components of operating income in detail, so some report data for "operational costs" that also includes non-tax transfers to government.

SOEs sometimes do not report dividend payments, making it unclear whether no dividends were paid or if they were classified under another category. Differences also exist between dividends reported on an accrual basis (linked to profit in the same year) and a cash basis (dividends paid in that year, often based on prior-year profits).

EXAMPLE

SNPC (Republic of the Congo): Note 34 "Fiche de synthèse des principaux indicateurs financiers" of SNPC's 2018 financial statements (p. 53) provides the value of dividends declared for 2017-2018, but confirms that no dividends were paid in cash in either year.

3. Government transfers to SOEs

Where to find information

Government transfers to SOEs are typically disclosed in the cash flow statement under "Financing Activities", and may be categorised as "grants", "assistance" or "other income from the state", among other labels.

How the EITI can add value

EITI reporting can:

- Clarify the flow of fiscal revenues collected by SOEs and their transfers to the Treasury.

- Provide insight on subsidies and financial relations within SOEs' subsidiaries, joint ventures and affiliates.

- Offer transparency on other payments and revenues outside regular legal frameworks, such as advances on fiscal payments.

EXAMPLE

Pemex (Mexico): Pemex's 2014 consolidated financial statements presents the value of financial transfers from the Federal Government, categorised as "Increase in equity due to Mexican Government contributions" under "Financing Activities" (pp. 7 and 102), with figures presented on an accrual basis.

Requirement 6.2: SOE quasi-fiscal expenditures

Quasi-fiscal expenditures are arrangements where SOEs undertake public social expenditure on behalf of the state that falls outside the formal government budget. This may include spending on social services, public infrastructure, fuel subsidies and national debt servicing.

Such expenditures are typically directed by the government, although in some cases individual government officials may issue directives that are not codified in law. Expenditures related to assets controlled or owned by the SOE that have not been directed by the government are usually not considered quasi-fiscal expenditures.[3]

EITI Requirement 6.2: Implementing countries are required to ensure SOEs disclose their quasi-fiscal expenditures. The multi-stakeholder group should establish a reporting process that aligns transparency around these expenditures with the disclosure of other payments and revenue streams, including those from SOE subsidiaries and joint ventures.

Where to find information

Consolidated financial statements typically do not explicitly identify quasi-fiscal expenditures. However, auditors may highlight them when the legal or contractual basis for such spending is unclear. In these cases, they may appear under the "expenditure" section of the income statement, although not specifically labelled as quasi-fiscal.

Expenditures for which SOEs expect reimbursement from the government may be disclosed as "related party transactions/balance", as the state is considered a related party to the SOE.

- **Social services:** SOE expenditures on social services may be reported under "expenditure" in the income statement but are rarely distinguished from other mandatory or voluntary expenditures.

- **Public infrastructure:** SOE expenditures on public infrastructure may be reported under "expenditure" in the income statement, especially when the amounts are significant, but such spending is often aggregated with other mandatory or voluntary expenditures and not highlighted in financial statements.

- **Subsidies:** Off-budget subsidies provided by SOEs (not reimbursed by the government) are generally only visible in the pricing of commodity sales to certain customers. These subsidies must be calculated based on differences between sales and market prices.

- **National debt servicing:** SOE payments toward sovereign debt are usually not reported as such in consolidated financial statements. Payments that are not reimbursed by the government typically appear in the financial statements of a subsidiary or special-purpose vehicle servicing the debt.

Gaps with EITI disclosure requirements

- **Social services and public infrastructure:** Consolidated financial statements typically do not disaggregate expenditures by project of type, meaning specific quasi- fiscal expenditures are often not visible.

- **Subsidies:** Subsidies are rarely highlighted as standalone costs unless they are reimbursed by the government. Off-market sales prices are generally only noted in audit reports.

- **National debt:** Payments for national debt servicing may involve deductions from the state's in-kind revenues that do not appear in SOE financial statements. In some cases, debt servicing is transferred to an SOE's subsidiaries, where revenues can be deducted to service the debt.

How the EITI can add value

EITI reporting can:

- Provides a framework for SOEs to clarify the non-commercial activities and costs they undertake, contributing to the public's understanding of SOEs' efficiency and profitability.

- Facilitate dialogue between SOEs, government (Ministry of Finance, line ministries), civil society and other stakeholders on the management of quasi-fiscal expenditures that fall outside the conventional budgetary process.

- Help countries demonstrate progress on benchmarks for international support programmes, such as those with the IMF.

EXAMPLES

- **OMNIS (Madagascar):** The 2018 audit report on raised concerns over MGA 7.58 billion in expenditures for constructing a highway to the capital's airport, directed by two government ministers. The auditor noted that this undermined OMNIS's autonomy.

- **SNIM (Mauritania):** SNIM directly financed the development of Nouakchott's airport and is being gradually reimbursed by the state through deductions from its royalty payments. These deductions are not reflected in the national budget. Note 4.3.1 "Investment in associate's entities" of SNIM's 2017 consolidated financial statements (p.27) describes this loan to the construction company.

- **Naftogaz (Ukraine):** Naftogaz supplies natural gas to power plants, religious organisations and households at prices below market value, as mandated by Ukrainian law. These sales are not compensated by the government, and Note 2 "Operating Environment" of Naftogaz's 2019 consolidated financial statements (pp. 18-19) describes the resulting off-budget subsidies.

Annexe A: Glossary of common terms in audited financial statements

Accounting policies: Accompanying a financial statement, the notes to the financial statements, provide details on the organisation's operations and the figures presented. Typically, the second note describes the organisation's accounting policies, which refer to the principles, practices and rules applied when preparing and presenting financial statements.

Auditor's report: An auditor's report is the formal opinion or disclaimer issued by an auditor after performing an audit. It confirms whether the financial statements are free from material error or omission. The auditor's report typically mirrors the structure of the financial statements and specifies whether errors or omissions that could impact the understanding of the financial statement were found.

Balance sheet: A balance sheet, also called "statement of financial position", is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific date. It helps compute rates of return and evaluate a company's capital structure.

Cash flow statement: A cash flow statement is a financial statement that summarises the amount of cash and cash equivalents entering and leaving a company. It shows how the company manages its cash, including debt obligations and operating expenses.

Cash-based vs accrual-based accounting: Cash-based accounting recognises revenues and expenses when cash is received or paid, while accrual-based accounting recognises income when it is earned and expenses when liabilities are incurred, regardless of cash flow.

Income statement: The income statement, also called "profit and loss (P&L) statement", is the most common financial statement and summarises a company's revenues, costs and expenses over a specified period, typically a fiscal quarter or year.

Joint ventures vs joint arrangements: A joint venture has rights to the net assets of the arrangements, while in a joint arrangement, the parties have rights to the assets and obligations for liabilities (see IFRS 11).

Materiality: Materiality refers to whether information is significant enough to influence decisions. Materiality can be quantitative or qualitative. A quantitative materiality consideration is usually a specific percentage of net income or other major financial aggregate (e.g. 5% of net income from continuing operations or 2-3% of operating income), but these thresholds can vary significantly. An item may not necessarily be considered as immaterial only because it falls below a predetermined quantitative threshold; other qualitative factors may still make an item material, such as misstatements that affect key ratios, or where statements distort transactions with related parties or other specific matters (see IFRS Materiality practice statement).

Ownership or interests in other entities: Ownership refers to the rights and responsibilities of the individuals holding a legal or equitable interest in a company. Ownership information helps users assess the risks and impacts of the company's interests in subsidiaries, joint arrangements or affiliates on its financial performance and position (see IFRS12).

Reinvestment vs investment: Reinvestment occurs when income from an investment is reinvested into that investment, such as dividends to buy more stock, or interest payments to buy more bond. This contrasts with general investments that involve fresh capital or purchasing assets.

Related parties: A related party is a person or an entity connected to the reporting entity. This includes close family members of an individual that has (sole or joint) control or influence over the entity, whether it is a parent company, subsidiary, fellow subsidiary, associate or joint venture of the reporting entity, or if it is (solely or jointly) controlled, or significantly influenced by a related party (see IAS24).

Retained earnings: Retained earnings are the portion of profits not distributed as dividends, kept for reinvestment or debt repayment. These earnings are reflected in the income statement and carried over to the equity section of the balance sheet, where they contribute to book value. Retained earnings (RE) are calculated as: RE = Period Start RE + Net Income/Loss – Cash Dividends – Stock Dividends.

Statement of shareholders' equity: This document highlights changes in stockholders' or shareholders' equity, or ownership interest in a company, from the start to the end of a given accounting period. It forms part of the company's balance sheet.

Stock: Stock represents shareholder equity. It is calculated as: Stock = Assets - Liabilities + Shareholder Equity (stock). Based on this equation, common stock is neither considered an asset nor a debt. However, being on the opposite side of the asset equation, it is treated more as a liability than an asset, as a shareholder can request to cash out.

Subsidiaries versus associates/affiliates: Affiliates and associates are companies where the parent company holds a minority stake, while subsidiaries are those where the parent company holds a controlling interest. Associates are entities over which the investor has significant influence, usually presumed if the entity holds 20% or more of the voting power, either directly or indirectly (e.g. through subsidiaries) (see IFRS IAS 28).

Third-party financing: Third-party financing occurs when SOEs secure financing from an external source, such as a bank or private investor, rather than from their shareholders or the state.

Endnotes

1 The guidance provided in this note is based on the assumption that SOE financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) issued by the IFRS Foundation and the International Accounting Standards Board (IASB). These aim to set internationally recognised accounting specifications and policies. See IFRS (n.d.), "List of IFRS Standards and IFRIC Interpretations", https://www.ifrs.org/issued-standards/list-of-standards/.

2 See IFRS (2017), "IFRS 11 Joint arrangements", https://www.ifrs.org/issued-standards/list-of-standards/ifrs-11-joint-arrangements/.

3 See more information in the EITI's guidance note on quasi-fiscal expenditures.

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