Extractive Industries Transparency Initiative

21ST EITI BOARD MEETING LUSAKA, 25-26 OCTOBER 2012

Validation Committee 8 October 2012

Board Paper 21-4-D

Secretariat review: Mozambique

For decision

Summary/Abstract

Subject to any further comments from the Mozambique MSG:

The Validation Committee recommends that Board designates Mozambique as EITI Compliant as of 26 October 2012.

EITI International Secretariat Ruseløkkveien 26, 0251 Oslo, Norway **www.eiti.org**
Tel +47 222 00 800 **Fax** +47 222 00 802 **Email** secretariat@eiti.org

SECRETARIAT REVIEW: MOZAMBIQUE

Recommendation

Subject to any further comments from the Mozambique MSG:

The Validation Committee makes the following recommendation to the Board:

> The EITI Board designates Mozambique as EITI Compliant as of *26 October 2012*. In accordance with the EITI Rules:
>
> - Mozambique must be revalidated within 5 years (i.e., by *26 October 2017*);
> - Stakeholders in the process may call for a new validation at any time within that period if they think the process needs reviewing;
> - Where valid concerns exist that a country has become EITI Compliant, but its implementation of the EITI has subsequently fallen below the standard required for Compliance, then the Board reserves the right to require the country to undergo a new validation or face delisting from the EITI; and
> - In accordance with the 2011 edition of the EITI Rules, Mozambique is required to produce EITI reports annually. EITI Reports should cover data no older than the second to last complete accounting period (i.e., Compliant countries must publish an EITI report by 31 December 2012 to meet the requirement for timely reporting).
>
> o In accordance with requirement 21(c), Mozambique is required to publish a public report annually on the previous year's activities, detailing progress in implementing the EITI and any recommendations from the validator.
>
> The Board congratulates the government of Mozambique for its sustained commitment and leadership of the EITI process. The Board also congratulates the Mozambique MSG for its efforts and effective leadership in EITI implementation. The Board calls on the government and multi-stakeholder working group to ensure that the Board's recommendations are implemented in full, and tasks the EITI International Secretariat with providing regular progress reports to the EITI Board.

SECRETARIAT REVIEW: MOZAMBIQUE

Contents

1 Executive Summary

In August 2011, the EITI Board established five corrective actions required for Mozambique to achieve Compliance. The Board subsequently granted Mozambique a waiver from undertaking a second validation[1], and tasked the International Secretariat with assessing whether the remaining EITI requirements have been met. The Secretariat's assessment is attached. In the Secretariat's view, all remedial actions have been completed and the outstanding requirements have been met. The draft Secretariat review was circulated to the Mozambique MSG on 1 October 2012. The Secretariat is awaiting comments.

[1] Ref. Board Circular 127, 10 July 2012

2 Introduction

Mozambique was admitted as an EITI Candidate Country on 15 May 2009. In February 2011, Mozambique's first EITI report was launched disclosing payments made by the major mining companies to government for 2008. On 30 March 2012, Mozambique published its 2009 EITI Report. MEITI has agreed terms of reference for the 2010 report (including a scoping report), and has appointed a reconciler with a view to completing the report by the end of 2012.

The Mozambique validation report was received in May 2011[2]. The international EITI Board subsequently declared that Mozambique had made "meaningful progress" in its implementation of the EITI, and, in accordance with the transition procedures, was given until 15 February 2013 to demonstrate compliance with the 2011 edition of the EITI rules[3]. The Board agreed that indicators 9, 11, 13, 14, and 15 were unmet, and agreed the following corrective actions were needed in order for Mozambique to achieve compliance:

1. The MSG should agree a clear definition of "material payments and revenues" and incorporate this definition into the reporting templates and reconciliation process for the second EITI Report (indicator 9). This should specifically address the question of the participation of small companies and social payments.

2. The second EITI Report should clearly demonstrate that all entities that make or receive material payments are participating in the reporting process (requirement 11).

3. As per the Indicator Assessment Tool for Indicator 13, the government and MSG should take steps to ensure that government disclosures to the reconciler are based on audited accounts to international standards and agree a strategy for addressing these issues in accordance with the requirements as specified in Validation IAT 13.

4. In accordance with the agreed definition of materiality (see point 1, above), the MSG should ensure that all material oil, gas and mining payments by companies to government are disclosed to the reconciler and incorporated into the second EITI Report (indicator 14).

5. In accordance with the agreed definition of materiality (see point 1, above), the MSG should ensure that all material oil, gas and mining revenues received by the government are disclosed to the reconciler and incorporated into the second EITI Report (indicator 15).

2 Mozambique's response to the Board decision

MEITI undertook a number of activities to address the four corrective measures agreed by the Board and comply with the unmet requirements (9, 11, 13, 14, and 15).

MEITI has submitted evidence[4] that these corrective actions had been undertaken as part of the second reporting process, including:

- MEITI conducted a scoping study to establish which revenue streams were material and consequently which companies and government entities should be covered in the EITI report. Based on the findings

[2] http://www.itie-mozambique.org/MEITI%20Validation%20report%20final%20140511%20(2).pdf (Portuguese).

[3] Ref. Board Circular 107 24 July 2011.

[4] Supporting evidence provided by the MSG are available on http://eiti.org/internal and include:
Annex B – Letter from Abdul Razak Noormahomed, Deputy Minister of Mineral Resources, on behalf of Mozambique EITI MSG.
Annex D – Mozambique EITI reconciliation report 2009
Annex E – Mozambique EITI scoping study

of the scoping study, MEITI agreed a clear definition of materiality and established a materiality threshold.

- Social payments were unilaterally disclosed in the 2009 EITI report.
- A schedule for the publication of the 2009 EITI report and an agreed timeline for the publication of the 2010 EITI report.
- Five material companies failed to report. The government has unilaterally disclosed the revenues from these companies. The revenues amount to 2.52 % of total government revenues.
- The government ensured that government reports were based on accounts audited to international standards by requesting the tax collecting entities (DGI, INP and IGEPE) to confirm in writing that the figures submitted for the EITI report were drawn from accounts that had been audited by the Administrative Court and the Mozambique National Auditors Office, which audit government accounts each year. The reconciler then checked each line of the reporting templates against the audited financial figures.
- The difference between the amounts declared by the companies and not reflected in the collections by the State as well as the amounts reported as having been received by the State Institutions but that were not reflected in the payments made by the companies amount to 625 221 MT [US$ 23 195], or less than 1% of total revenues. MEITI ensured that all reporting entities comprehensively disclosed all material payments and revenues.

Based on the above, on 18 May 2012 Abdul Razak Noormahomed, Deputy Minister of Mineral Resources and MEITI Chairperson, wrote to the EITI Board to request a Secretariat Review on behalf of the whole MSG. On 20 July 2012, the EITI Board granted Mozambique a waiver from undertaking a second Validation[5]. The Terms of reference for the review are presented in annex C. The EITI International Secretariat conducted a desk review in July-August 2012. During the review, MEITI stakeholders were consulted and given an opportunity to share their views.

3 Secretariat review of remedial actions and assessment of indicators

The EITI Board agreed five remedial actions and tasked the Secretariat with reassessing compliance with Requirements 9, 11, 13, 14, and 15.

3. 1 Remedial action 1

The MSG should undertake an improved scoping and clarification of the receipts/payments to be included in future EITI reconciliations including a clear definition of "material payments and revenues" and incorporate this definition into the reporting templates for the second EITI Report (requirement 9). This should specifically address the question of the participation of small companies and social payments.

Validator's findings

The validator noted that there was evidence of discussion by the MSG of which payments should be covered in the EITI report and that these were "related to license fees, surface tax, royalties, profit tax and dividend and all other payments made by the companies to the government or as social fund should be mentioned in the report separately". However, the revenue streams discussed by the MSG differed from the revenue streams that were included in the ToRs for the reconciler, and the Validator did not obtain evidence that that the final reporting templates were agreed by the MSG.

[5] Annex C – Board decision on Mozambique's Validation waiver request, Board Circular 127, 10 July 2012, including Terms of reference for the Secretariat Review, available from http://eiti.org/internal.

The Validator reported that the MSG later agreed a minimum materiality threshold of 1.5 million MZN (USD 50,000). The rationale for establishing the threshold at this level was unclear. The threshold was also agreed after the reconciliation process had begun, reducing an initial list of 23 reporting companies to 6 reporting companies. MEITI confirmed that the combined payments from the remaining companies exceeded the minimum materiality threshold and that the full inclusion of social payments, as agreed by the MSG, would have meant that more companies should have reported.

With regards to social payments, the validator noted that the MSG agreed to include social payments in the report for information purposes. According to the validator, it was unclear why these were excluded from the TORs for the reconciler and from the report in the end. There were expectations from MSG members that these would be included, even after the reconciler had been appointed (Validation report, p.35).

Progress since Validation

MEITI conducted a scoping study[6] to establish which revenue streams were material, and consequently which companies and government entities should be covered in the EITI report. Based on the findings of the scoping study, MEITI agreed a clear definition of materiality that covered eight revenue streams, drawing on information collected from various Government agencies (General Directorate of Taxes, Ministry of Finance, the National Directorate of Mines and the National Petroleum Institute). These revenue streams include signature bonuses, but the MSG has confirmed that there were no signature bonuses paid in 2009.

MEITI established a materiality threshold of 500 000 MT (appx. US$ 16,500) for mining companies. 24 mining companies made payments above this threshold in 2009 and were requested to report. Payments from these companies represented 92% of revenues from the mining sector. The remaining revenues from the mining sector come from payments made by 72 small mining companies. The revenues from these non-material companies are disclosed in the annexes to the scoping report[7].

All hydrocarbon companies were requested to report, regardless of the size of their payments. According to the scoping report, twelve hydrocarbon companies made payments in 2009 and were requested to report.

The scoping report identified seven taxes collected at municipal level. According to the report 'municipal taxes and fees were not being considered as these represent local government revenues (municipalities). These are public legal persons that are distinct from the State, have the authority to collect revenue in the areas of their jurisdiction and what is known is that they are in the phase of organising their system of revenue collection' (Scoping report, p.10). Apart from license fees, the local taxes are not specific to the extractive industries.

Social payments are unilaterally disclosed in the 2009 EITI report.

Secretariat's Assessment

The Secretariat has reviewed the scoping study and the 2009 EITI report and is satisfied that MEITI has agreed a clear definition of materiality. Participation of small companies has been addressed by establishing a materiality threshold that appears reasonable (500 000 MT / US$ 16 500 for mining companies and 0 for hydrocarbon companies). The approach for covering social payments is clear.

Total revenue from material companies in the scoping report differs slightly from total revenue in the EITI

[6] Mozambique Scoping study, available from http://www.eiti.org/internal and at http://www.itie-mozambique.org/Scoping%20Study%20II%20EITI%20Report.pdf.

report, especially for two companies that reported 230m MT more than was indicated in the scoping report. This is because, due to time constraints, the scoping report only included figures from those revenue collection agencies that are linked to the central database. Some companies paid some to revenue collection agencies that are up-country and not electronically linked. In the reconciliation report, all revenue collection bodies were included. This approach was approved by the MSG.

The EITI International Secretariat is satisfied that the remedial action requested by the Board has been completed.

3.2 Remedial Action 2

The second EITI Report should clearly demonstrate that all entities that make or receive material payments are participating in the reporting process (requirement 11).

Validator's findings

The validator did not access the mining and petroleum laws and was therefore unable to assess whether all companies that made material payments and should have participated in the 2008 EITI report, did so. The absence of a clear definition of materiality also made it impossible to establish which companies should have reported.

Progress since Validation

According to the 2009 report, 24 mining companies met the materiality threshold and were asked to report. 20 of these companies reported. The four mining companies that failed to report all made payments in 2009 that exceeded the materiality threshold. Two of the companies – JSW Natural Resources Mozambique Lda and Africa Drilling company/Afrodroll - did not report because they were no longer present in Mozambique. The other two companies – AP Capidal Lda and Grinaker Mocambique Lda - did no longer hold mining licenses, but were fined 70 000 MT for not complying with the reporting requirement. Of the twelve hydrocarbon companies that were considered material, eleven reported. One company – Wentworth Mocambique Petroleos Lda failed to report because it was no longer operating in the country.

The combined contribution of these five companies represents 2.52 % of total revenues collected in 2009. The figure is unilaterally disclosed (in aggregate) in the EITI report by the government (EITI report, p. 19-20). The breakdown per company is not included in the EITI report, but is provided in the scoping report (annex 3). The size of their individual payments was less than 1% of total revenues for each of the five companies.

All government agencies at central level that collected material revenues reported. According to the scoping report, seven revenue streams were collected at subnational level. Of these, only license fees are related to the extractive industries. However, license fees were only collected by the subnational government as a collecting entity on behalf of the central Ministry of Finance. They were thus covered in the EITI report as payments to central government. In the reporting template, there was no entry for license fees, so it is not possible to tell if they were material in their own right or not[8]. However, as they were included by companies under "surface taxes" or "other taxes paid", they were not excluded.

---

[8] The payments were likely to have been immaterial. This is because license fees vary from 10 Mt/km^2 (approx. US $0.33) to 50.000 Mt/Km^2 (approx. US $1,666) per year. This means that a company would need a concession of between 10 Km^2 to 50,000Km^2 to be approaching materiality. Given the size of mining concessions in Mozambique, this is highly unlikely.

Requirement 9(e) states that "where material, the MSG should take steps to ensure that the reconciliation of company payments to subnational government entities and the receipt of these payments is incorporated into the EITI reporting process". The template for the third report will include license fees as a separate item.

Secretariat's Assessment

Five companies that made payments above the materiality threshold failed to report. Revenues from these companies are unilaterally disclosed by the government in the EITI report and the implication of the omission on the comprehensiveness of the report (2.52% of total revenues) has been established. Of the companies that did not reply to the reporting templates, three were either no longer operating in the country, and the other two were fined 70 000 MT. One paid and the other sent acceptable evidence that they had sent the information to a wrong destination.

The Secretariat therefore concludes that payments made by the five non-reporting companies did not materially affect the EITI report.

Whilst the Secretariat is satisfied that the license fees collected at the subnational level were covered in the report, the EITI process would benefit from additional clarity on these issues, including a more detailed explanation of the payments and revenues collected at sub-national level.

The EITI International Secretariat is satisfied that the remedial action requested by the Board has been completed.

3.3 Remedial Action 3

As per the Indicator Assessment Tool for Indicator 13, the government and MSG should take steps to ensure that government disclosures to the reconciler are based on audited accounts to international standards and agree a strategy for addressing these issues in accordance with the requirements as specified in Validation IAT 13.

Validator's findings

The Validator noted that government agencies in Mozambique were audited by an independent audit agency which follows INTOSAI rules. AFROSAI-I rules were also applicable to Mozambique. There was no evidence that the data disclosed by the government for the purpose of the EITI report had been audited to international standards, nor did the Validation report present the reconciler's views on the reliability of government data.

Progress since Validation

The Administrative Court and the Mozambique National Auditors Office audit all government agencies. The government ensured that government reports were based on accounts audited to international standards by requesting the tax collecting entities (DGI, INP and IGEPE) to confirm in writing that the figures submitted for the EITI report were drawn from accounts that had been audited by these bodies. The reconciler confirms that 'the State institutions selected for the gathering of the information, namely DGI, INP and IGEPE, provided the data requested by means of formal letters signed by the individuals responsible' (EITI report, p. 48). In addition, DGI which is the entity that collects the largest amount of revenues provided a print out of the receipts directly extracted from the tax collecting system, enabling the reconciler to confirm the information contained in the templates. The reconciler noted that 'this procedure gave us the required comfort for the undertaking of the work as the information in the print outs matches with the information provided by the companies, in terms of dates, reference numbers and amounts. Without prejudice to the issues raised under recommendations, we considered that the information provided by the State institutions, particularly by DGI is reliable' (EITI report, p.48).

Secretariat's Assessment

The Secretariat's assessment is that the MSG has agreed a reasonable approach for ensuring that government disclosures to the reconciler are based on accounts audited to international standards. We have also reviewed requirement 12 to check if the process agreed by the MSG was followed. Although not all the templates were signed by external auditors, they were at least signed by senior officials (accountants and or managers). This approach to ensuring reliable company data was agreed by the MSG.

The EITI International Secretariat is satisfied that the remedial action requested by the Board has been completed.

3.4 Remedial Action 4

In accordance with the agreed definition of materiality (see remedial action 1, above), the MSG should ensure that all material oil, gas and mining payments by companies to government are disclosed to the reconciler and incorporated into the second EITI Report (indicator 14).

Validator's findings

The Validator reported that the MSG agreed a minimum materiality threshold of 1.5 million MZN (USD 50,000) for the 2008 EITI report. The rationale for establishing the threshold at this level was unclear. The threshold was also agreed after the reconciliation process had begun, reducing an initial list of 23 reporting companies to 6 reporting companies. MEITI confirmed that the combined payments from the remaining companies exceeded the minimum materiality threshold and that the full inclusion of social payments, as agreed by the MSG, would have meant that more companies should have reported.

Progress since Validation

As noted above, five material companies failed to disclose their payments to the reconciler. The payments amounted to 2.52 % of total payments.

According to the 2009 EITI report, the discrepancy resulting from tax payments not reported by extractive companies amounted to 20 848 945.96 MT (US$ 773 495) and amounts received by the state and not reported amounted to 40 938 766.72 MT (US$ 1 518 828). The reconciler notes that 'with respect to the amounts paid/received and not reported, the large majority of the amounts assessed results, on the one hand, from the non-inclusion of the payments made in January 2009 (referent to the tax return for December 2008) and, on the other, the non-transition of the amounts contained in the payment forms/reports of the receivals by the enquiring party' (EITI report, p.46). The net prevailing difference represents only 0.06 % of revenue reported by the State.

Secretariat's Assessment

The EITI International Secretariat is satisfied that the remedial action requested by the Board has been completed.

3.5 Remedial Action 5

In accordance with the agreed definition of materiality (see remedial action 1, above), the MSG should ensure that all material oil, gas and mining revenues received by the government are disclosed to the reconciler and incorporated into the second EITI Report (indicator 15).

Validator's findings

The Validator stated that 'there is no any evidence of the completeness of the information received from the government agencies' (Validation report, p.41). The Validator gave examples of how some benefit streams such as concession fees and profit taxes were not recorded on government templates. Stakeholders agreed that there were significant difficulties with regards to data collection from the Ministry of Mineral Resources and the Revenue Authority/Ministry of Finance.

Progress since Validation

The government disclosed revenues from all but one company, Opti Metal Trading Mozambique. The payments declared by this company amount to 635 489.86 MT (US$ 23 576), which are exploration/prospecting fees and environmental license. This payment amounts to 0.0006% of total revenues.

According to the 2009 EITI report, the discrepancy resulting from tax payments not reported by extractive companies amounted to 20 848 945,96 MT (US$ 773 495) and amounts received by the state and not reported amounted to 40 938 766,72 MT (US$ 1 518 828). The reconciler notes that 'with respect to the amounts paid/received and not reported, the large majority of the amounts assessed results, on the one hand, from the non-inclusion of the payments made in January 2009 (referent to the tax return for December 2008) and, on the other, the non-transition of the amounts contained in the payment forms/reports of the receivals by the enquiring party' (EITI report, p.46). The net prevailing difference represents only 0.06 % of revenue reported by the State.

Secretariat's Assessment

The EITI International Secretariat is satisfied that the remedial action requested by the Board has been completed.

4 Conclusion

The Board decision stipulated that five remedial actions should be completed in order for Mozambique to achieve Compliance. The International Secretariat is satisfied that the remedial actions have been satisfactorily completed and that the outstanding requirements are met.

Annex A - Board decision on Mozambique, Board Circular 107, 24 July 2011

The Board concludes that Mozambique has made meaningful progress in implementing the EITI. The Board agreed that Mozambique would retain is status as a Candidate country, subject to a clearly defined and agreed work plan for achieving Compliant status, including a schedule for its next Validation.

The Board congratulates the government, companies and civil society organisations in Moazmbique for the progress made in implementing the EITI. It especially notes the production of the first MEITI Report in January2011. The Board also wishes to congratulate the validator and all stakeholders involved in the validation process on a clear and validation comprehensive report.

The validator found that Mozambique has not met a number of the validation indicators. The validator expresses concerns about the lack of an updated workplan, lack of civil society engagement and lack of disclosure of government revenues to the reconciler.

In all decisions on Validation the Board places a priority on the need for comparable treatment between countries and the need to protect the integrity of the EITI brand. The Board reviewed the validator's report in detail. On several issues, the Board shares the validator's concerns. However, the Board also disagreed with some of the validator's assessments. The Board agreed that indicators 9, 11, 13, 14, and 15 are unmet, and agreed the following corrective actions needed in order for Zambia to achieve compliance:

1. *The MSG should agree a clear definition of "material payments and revenues" and incorporate this definition into the reporting templates and reconciliation process for the second EITI Report (indicator 9). This should specifically address the question of the participation of small companies and social payments.*

2. *The second EITI Report should clearly demonstrate that all entities that make or receive material payments are participating in the reporting process (requirement 11).*

3. *As per the Indicator Assessment Tool for Indicator 13, the government and MSG should take steps to ensure that government disclosures to the reconciler are based on audited accounts to international standards and agree a strategy for addressing these issues in accordance with the requirements as specified in Validation IAT 13.*

4. *In accordance with the agreed definition of materiality (see point 1, above), the MSG should ensure that all material oil, gas and mining payments by companies to government are disclosed to the reconciler and incorporated into the second EITI Report (indictor 14).*

5. *In accordance with the agreed definition of materiality (see point 1, above), the MSG should ensure that all material oil, gas and mining revenues received by the government are disclosed to the reconciler and incorporated into the second EITI Report (indictor 15).*

The Board recommends that the MSG should agree a comprehensive (time-bound and costed) work plan that: (1) covers the publication and dissemination of the second EITI report and steps toward regular and timely EITI reporting thereafter; (2).addresses on the recommendations from the first reconciliation report and from the validator; and (3) addresses the corrective actions highlighted above.

In developing the workplan, the Board also recommends that the government and the MSG formally assesses whether there are any barriers to achieving compliance (including capacity constraints, and any legislative or regulatory barriers). Furthermore, it is suggested that the MSG revises its Terms of Reference based on the lessons learned from the first EITI Report and the validation process in order to secure effective governance and oversight of the MEITI process.

In accordance with the transition procedures, the Board agreed that Mozambique will have its candidacy renewed for 18 months (i.e. until 15 February 2013) by the end of which it must have completed a Validation that demonstrates compliance with the 2011 edition of the EITI rules. If Mozambique does not achieve compliant status by this deadline it *will be de-listed.*

The MSG may request a waiver from the requirement to undergo a second Validation on the grounds that the remedial actions necessary for achieving compliance are not complex and can be undertaken quickly. It will be within the discretion of the Board to determine whether to grant the waiver request. If the waiver request is made in 2011 and subsequently granted, the secretariat review will be conducted in accordance with the old rules regardless of the date of the Board decision.

Annex B – Letter from Abdul Razak Noormahomed, Deputy Minister of Mineral Resources, on behalf of Mozambique EITI MSG.

Available from http://eiti.org/internal

Annex C – Board decision on Mozambique's Validation waiver request, Board Circular 127, 10 July 2012, including Terms of reference for the Secretariat Review.

Available from http://eiti.org/internal

Annex D – Mozambique EITI reconciliation report 2009

Available from http://eiti.org/internal

Annex E – Mozambique EITI scoping study

Available from http://eiti.org/internal