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Members of Congress, Ladies and Gentleman, I am honored you have invited me to express my views on H.R. 6066, the Extractive Industries Transparency Disclosure Act (the EITDA). I am eager to answer any questions you may ask me as a Professor of Law specializing in corporate governance and securities regulation.

As you know, the Act you are vetting today would require enhanced informational disclosure by international extractive enterprises having a sufficient U.S. presence so that they or their affiliates fall under the SEC's periodic reporting requirements. In particular, the Act calls for such firms to make annual, publicly searchable reports to the SEC of all payments they've made to foreign governments for natural resources and extraction rights, with the exception of payments less than $100,000.

Such enhanced informational reporting would allow current and prospective investors in covered companies better to evaluate the natural resources and rights which their firms have obtained, as well as the costs and potential risks, legal as well as economic, incurred in obtaining them. In this manner, the Extractive Industries Transparency Disclosure Act would empower individual shareholders and the securities market in general better to evaluate the risk/reward profile of individual extractive projects, and better to compare different projects within and among companies covered by the Act. In addition, the Act would enhance covered companies' incentives to comply with the existing legal prohibitions against off-the book payments and bribes, and would enhance law abiding covered companies' ability to attest to the legitimate, genuinely negotiated, market-based terms of the natural resource rights in foreign countries.

The Act is consistent with Congress' broader objectives in regulating interstate commerce and overseeing the system of public reporting to investors – *viz.* enhancing market efficiency, sustaining current levels of market liquidity and empowering and protecting U.S. investors. As would the Act, the SEC's periodic reporting requirements extend to U.S. and also foreign corporations which have raised capital in SEC-registered public offerings, have listed securities on any U.S. exchange or have surpassed minimum numbers of record shareholders and asset values in the U.S. In regard to the Act's substance, the disclosures it would require are, in effect, precise applications of already existing, more generalized disclosure mandates arising under the headings of "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations," as well standards of "quantitative materiality" endorsed by the SEC (as defined in SEC Staff Accounting Bulletin No. 99 (dated August 12, 1999)).

The Act would benefit investors by facilitating their ability to value the covered companies' natural resources rights and contracts, and the financial and legal risks attaching to them. In addition, increasing investors' confidence that they have the information reasonably necessary to price such natural resource rights and contracts should help lower covered companies' costs of capital. As it would foster U.S. investors' confidence in investing in international extractive industries, Congress' enactment of the EITDA would help to sustain the valuable liquidity present in this area of the U.S. securities markets. And the additional disclosures contemplated in the EITDA would contribute to the markets' ability more rationally to price the securities of covered companies.

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Furthermore, the Act would help to reinforce corporate senior executive officers' fulfillment of their duties of care, loyalty and good faith – that is, their fiduciary obligations arising under state corporation law. To clarify, by enacting the EITDA into law, Congress would encourage senior corporate executives to exercise their utmost diligence, loyalty and good faith in negotiating for and capitalizing on the value of their companies' natural resources rights -- since it's logical that managers most efficiently and faithfully manage resources which they are obliged to account for publicly.

The disclosure which would be mandated by the Act would enhance investors' ability to judge whether a covered companies' executives have endeavored to hide or obscure legal and financial risks related to their foreign natural resource rights. In cases where evidence of some questionable transactions or questionable reporting practices was evident, investors could make informed judgments about their risk tolerance, and the securities markets would (consistent with the concept of efficient markets) impound such new information into the price of the covered companies' securities. Investors who concluded that their securities were overpriced or vulnerable to future losses could resolve to sell and "cut their losses." In addition, by fostering early detection of questionable natural resource related payments or transactions, the Act would allow shareholders to agitate for corporate reform early on -- before the company's overall reputation and financial health was impaired. Furthermore, the disclosures mandated by the Act would help investors to evaluate the overall quality of the business judgment and professional integrity of covered companies' senior executive officers – which should be a material factor influencing investors' decisions to buy, sell or hold securities.

Recent domestic and international legal developments raise the litigation-related costs for extractive firms implicated in illicit transactions with foreign governments. In this regard, the Act would shed light on a facet of international corporate transacting that increasingly exposes U.S. investors to substantial, difficult to quantify litigation-related financial risk and costs. Faithful reporting under the EITDA would help law abiding covered companies immunize themselves from serious legal claims. By allowing for better verification that covered companies have obtained their rights to foreign-based natural resources through lawful, market-based negotiations and agreements with the foreign country's officials, the EITDA would enhance investors' confidence about the enforceability of their firms' foreign-based natural resource rights and contracts. To clarify, the reports which would be mandated by the EITDA would help investors better evaluate whether their company's rights are unassailable and safe from expropriation by foreign governments claiming illegality, fraud or other serious abuses. Once again, the disclosure contemplated by the Act would foster investors' opportunities to make informed investment choices. In addition, it would foster law abiding, "market-transacting" firms' ability to profit from the enhanced investor confidence they would foreseeably garner from complying with high ethical standards and legally mandated reporting requirements in regard to their foreign transactions in natural resources rights.

Furthermore, because covered companies' could use good faith reporting under the EITDA to help attest to the propriety of their foreign transactions in natural resource rights, these reports might represent a low cost means of protecting these companies against "globalization backlash" and the wide ranging, heightened conduct-based regulatory requirements it might inspire. Such expanded regulatory requirements would foreseeably exceed the minimal administrative and reporting costs which would arise under the EITDA. By negative comparison with covered, reporting firms, if enacted, the Act would stigmatize extractive companies which refused to or failed to make credible, comprehensive, verifiable disclosures of the data called for thereunder. Again by negative implication, investors would become sensitized to the greater risks associated with investing in firms which refused to or failed to make the disclosures contemplated by the EITDA.

The EITDA is well drafted – it should broadly accomplish its goals at low cost. First, in terms of its efficacy, the Act would be extraordinarily comprehensive in its coverage. According to data compiled by Publish What You Pay, it would reach at least 90% of the major companies active in international natural resource extraction – that is, very few major extractive enterprises doing business internationally would fall outside of the Act's mandatory disclosure requirements. Hence, only a very small population of major international extractive firms would be in a position even to attempt to garner a comparative advantage from maintaining the confidentiality of their foreign transactions in natural resource rights. (The comparative advantage/disadvantage issue is addressed further below in this Testimony's concluding remarks.)

In regard to the burdens it would impose, most importantly, apart from its newly expanded disclosure requirement, the Act proposes no new conduct requirements or conduct prohibitions on extractive enterprises. Corporate acts and transactions which were already unlawful remain unlawful. And leaving aside (non)disclosure, corporate acts and transactions which were lawful remain lawful.

Nor, even, would the additional mandatory disclosures contemplated by the Act give rise to new information gathering costs for U.S. reporting firms – since any reasonably efficient international business would presumably have the relevant information called for by the Act readily at hand. For the most part, the Act would not even require new oversight or compliance measures or systems of verification. This is because the accurate reporting of transactions and maintenance of internal controls procedures sufficient to produce accurate corporate books and records was made mandatory for SEC reporting companies more than thirty years ago by Congress' enactment of the books and records provisions of the Foreign Corrupt Practices Act (as codified in Section 13(b) of the Securities and Exchange Act). And Congress has consistently reinforced this emphasis on accurate corporate reporting and effective corporate auditing – for example by enacting the Sarbanes-Oxley Act, and the USA PATRIOT Act.

You will undoubtedly consider certain superficially worrisome but ultimately insubstantial critiques of the Act. You may ask why, if disclosure is good for companies and shareholders, we cannot rely on corporate managers voluntarily to provide it to shareholders? The answer -- as we are more mindful after the fall of Enron and WorldCom – is that managers may fail to disclose corporate information for self-serving reasons. They may be inclined to use material nonpublic information to profit from trading on undisclosed or selectively disclosed good or bad news. (The limited budgetary resources of the SEC ensures that not all illicit trading by senior executives will be detected or redressed.)

Even more importantly, corporate senior executives would naturally prefer to minimize and obscure the importance of unfavorable events and transactions which would cast doubt on the quality of their leadership and business judgment. This insight points to the EITDA's relationship to the basic architecture of corporate and securities law. The American corporate governance bargain is that managers and not shareholders get to make business decisions and investors cannot second-guess managers' lawful business judgments made in good faith. The flip side of this bargain however, as enforced by the federal securities laws and regulations, is that shareholders must be afforded detailed, accurate information about the firm's assets, operations and financial condition -- information illustrative of the quality of their managers' decision making and professional integrity -- so that they can make informed choices about buying, selling or holding their securities. In this regard, the informational disclosure contemplated by the EITDA fits neatly into the broader scheme of U.S. corporate and securities laws.

Voluntary disclosure has several other essential defects. First, of course, companies can simply ignore voluntary disclosure mandates. Furthermore, an informational environment filled with spotty, unreliable and incomplete disclosures undermines the usefulness of even reliable reports which investors might voluntarily receive. Disclosure that is voluntary will inevitably be uneven and ad hoc – in essence, impressionistic. For this reason, it will not allow for meaningful comparability – which is to say will not accomplish meaningful transparency -- among and between extractive companies and projects.

In addition, investors and the marketplace will inevitably discount the credibility and accuracy of disclosures which are merely voluntary in nature. The marketplace cannot adequately distinguish between earnest voluntary disclosure and self-serving, potentially misleading corporate "spin." For this reason, companies cannot use voluntary publicity to garner the full financial benefits which would accrue from their making systematic, legally mandated disclosures. Furthermore, by enacting the EITDA into law, Congress can signal to companies and investors, as well as broader constituencies, the seriousness of the principles at stake in achieving greater transparency in regard to international natural resource transactions.

It is also crucially important to consider the enforcement mechanisms contemplated – and not contemplated – by the Act. In particular, the Act does not contemplate a private cause of action for companies' failure to supply the information mandated thereunder. In this regard it is consonant with recent Acts of Congress which have reflected concern about the costs which may be imposed on businesses by vexatious private suits.

Nor would the broader framework of private remedies for securities fraud afford a basis for suits by investors. In particular, the limits and safeguards which Congress, the SEC and the federal courts have imposed on private investor suits for fraud -- for example, heightened pleading requirements and proof of loss causation and scienter – would effectively preclude investors from using the existing antifraud prohibitions under the federal securities laws to bring claims alleging deficient EITDA reporting.

In the alternative, enforcement of the Act's disclosure requirements would fall to the discretion of the SEC, under the oversight, in most cases, of the federal courts. Most notably (leaving aside cases of notorious, repeated, material disclosure deficiencies, gross financial frauds and instances of market manipulation and insider trading), SEC enforcement actions rarely have resulted in substantial corporate fines or penalties. In responding to perceived shortcomings in the kind of reporting contemplated under EITDA, the SEC has most commonly sought civil injunctions or obtained consent decrees prohibiting future disclosure violations. Moreover, even if the SEC succeeds in proving a claim of materially deficient reporting in federal court (monetary fines against reporting companies are unavailable in administrative actions), Section 21(d) of the Securities Exchange Act of 1934 establishes a three tiered system of fines and penalties which caps the remedies which the SEC may obtain – again, absent egregious facts or fraudulent or repeated reckless disclosure deficiencies – at $50,000 per corporate violation.

One final important critique of the Act should be addressed – that is, the issue of whether the EITDA would confer a comparative advantage on companies falling outside its reach. Certain features of this critique have been addressed previously -- most importantly, that very few major, international extractive enterprises would fall outside of the Act's disclosure requirements. Secondly, the above discussion highlighted how investors – and hence companies seeking to raise capital at efficient prices and the securities markets in general – stand to benefit from the disclosures which would be legally mandated by the Act's passage. Furthermore, that certain firms might fall outside of the EITDA – even that certain firms fall outside of the scope of the U.S. securities laws in general – is a poor rationale for endorsing lax U.S. standards and requirements. That is, the United States has long been a leader in advocating standards of good corporate governance, and systems of accurate corporate reporting – and these standards and requirements have helped keep our markets strong and stable, have supported capital formation and protected investors' faith in investing.

As it turns out, moreover, the comparative disadvantage argument is inherently shaky. Its fatal flaw is that truly repressive foreign governments are unlikely to make decisions about which businesses to transact with based on the presence or absence of the kind of reporting requirements contemplated by the EITDA. Governments which have histories of high levels of corruption and which are likely to demand off-the-books payments in connection with the sale of resource rights are unlikely to be substantially affected by whether the terms of such transactions are subject to a publicly searchable filing with the SEC.

Second, regarding the issue of comparative disadvantage, if companies subject to U.S. reporting requirements pay bribes to foreign officials or engage in off-the-books transactions in obtaining natural resource rights, they are breaking U.S. federal laws which predate the EITDA. If companies cannot do business in conformity with the limits and standards established by Congress, then they should address this broader issue directly, rather than under cover of opposing the EITDA. Congress' consideration of the EITDA should not become a tacit vehicle for backing away from the anti-bribery, anti-money laundering and anti-corruption/national security laws which it has previously enacted.

This testimony has described how the passage of the EITDA might afford companies who embrace its disclosure mandates a comparative advantage in attracting publicly traded equity capital. Indeed, such companies should be more likely not only to attract public equity capital at favorable rates, but also private equity capital and debt financing, private and public. The reporting requirements contemplated by the Act are consonant with Congress' and the SEC's longstanding commitment to enhancing market efficiency and the rule of law underpinnings of free markets in general. In conclusion, the enactment of the Extractive Industries' Disclosure and Transparency Act would advance the welfare of U.S. investors and the market for securities of SEC reporting companies involved in international natural resource extraction, while imposing little cost on the firms it governs.