

Enhancing Oil Sector Governance in Nigeria through Transparency Reforms

CSEA Economic Policy and
Fiscal Strategy Seminar
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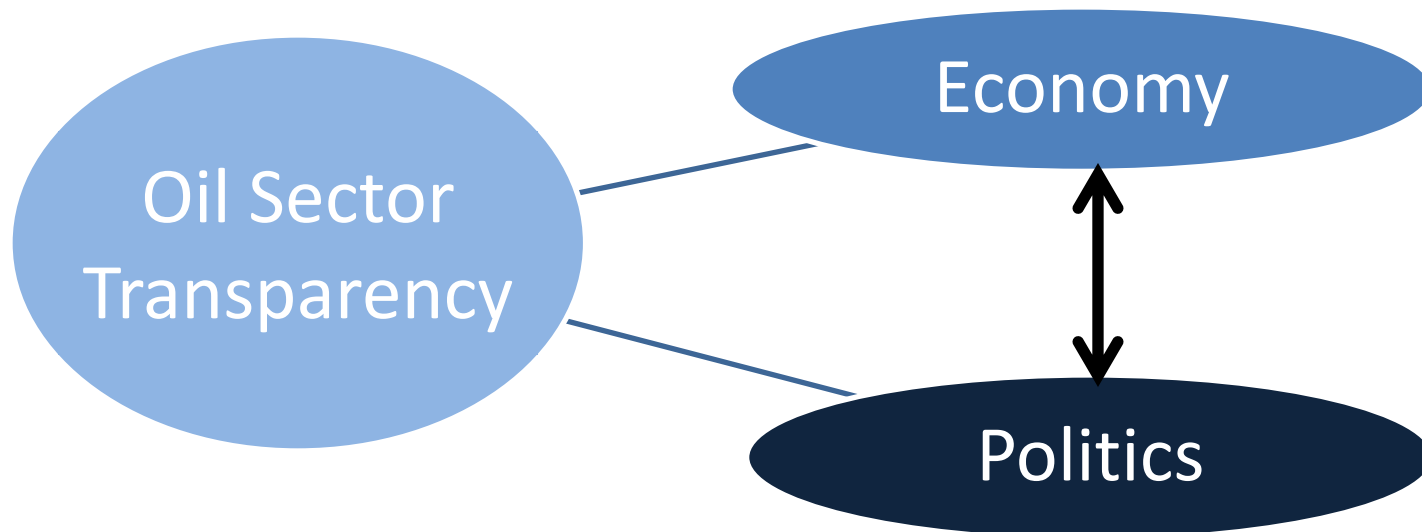
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Outline

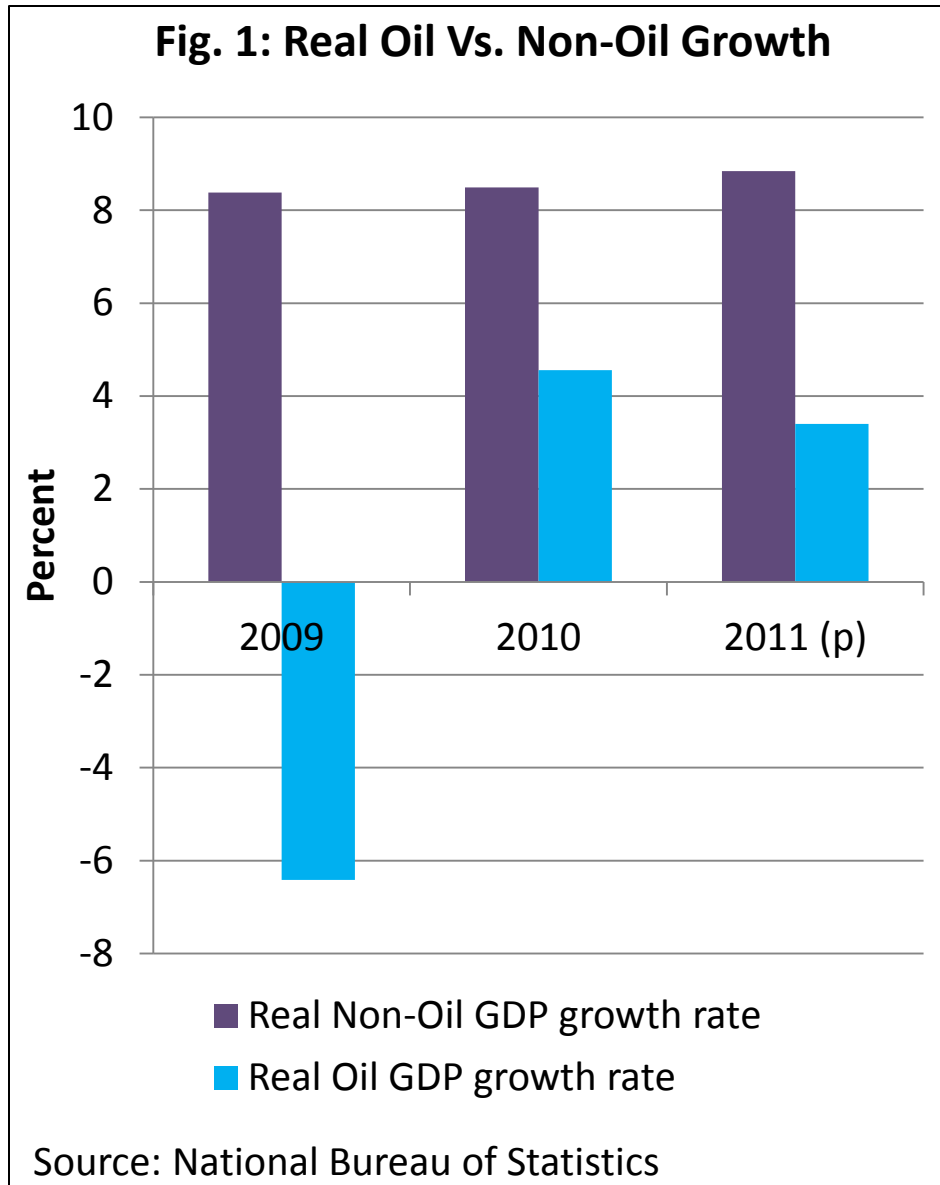
- Introduction: Why does oil sector transparency matter?
- Oil sector transparency actors
- The *Oil Corruption Pipeline*
- The PIB, oil sector governance and transparency reforms
- Discussion

Why Oil Sector Transparency?

- Corruption negatively affects growth. Overriding logic of unproductive rent-seeking in Nigeria's political economy
- Transparency reforms needed to shore up the credibility of the oil sector, and enhance productivity and efficiency
- Greater oil sector transparency will support the government's push towards structural reforms and inclusive growth



Oil Sector Performance



- Real Oil GDP growth was - 6.42% in 2009, and increased to 3.4% in 2011.
- The oil sector has experienced negative growth and is growing slower than the non-oil sector.
- In 2011, real oil GDP growth will be less than half of projected non-oil growth.
- This growth trend reflects structural inefficiencies, the Niger Delta crisis and corruption, which have reduced the productivity and growth of the oil sector.
 - Imperative of structural reforms to boost oil sector performance

Political rationale for oil sector transparency

- Oil sector corruption reduces state revenues, triggers factional (resource) conflicts within the political elite and undermines the credibility of political leaders
 - Need for stability, credibility and certainty in oil sector governance
 - Oil sector transparency reforms will strengthen institutions and provide a broad framework for political transformation
- Foreign capital is now seeking more ‘secure’ extractive locations in Africa (such as Angola)
- Arab Spring and unsettled global energy markets provide unique opportunity for Nigeria to leverage its regional and global influence by repositioning the oil sector

A sound, robust oil sector is premised on transparency, accountability and efficiency

Oil sector transparency actors

- These are the state institutions that have a statutory responsibility related to a specific area that affects oil sector transparency
- Complexity of oil activities requires broad-based approach to identify transparency actors

NNPC
DPR
Ministry of Petroleum
NAPIMS
Ministry of the
Environment

Oil industry operations

Ministry of Finance
Central Bank of Nigeria
FIRS
Sovereign Wealth Fund

Oil revenue management

NEITI

Oil transparency
watchdog

Budget Office of the Federation
Office of the Accountant-General of
the Federation
Revenue Mobilisation, Allocation
and Fiscal Commission

Oil revenue allocation and distribution

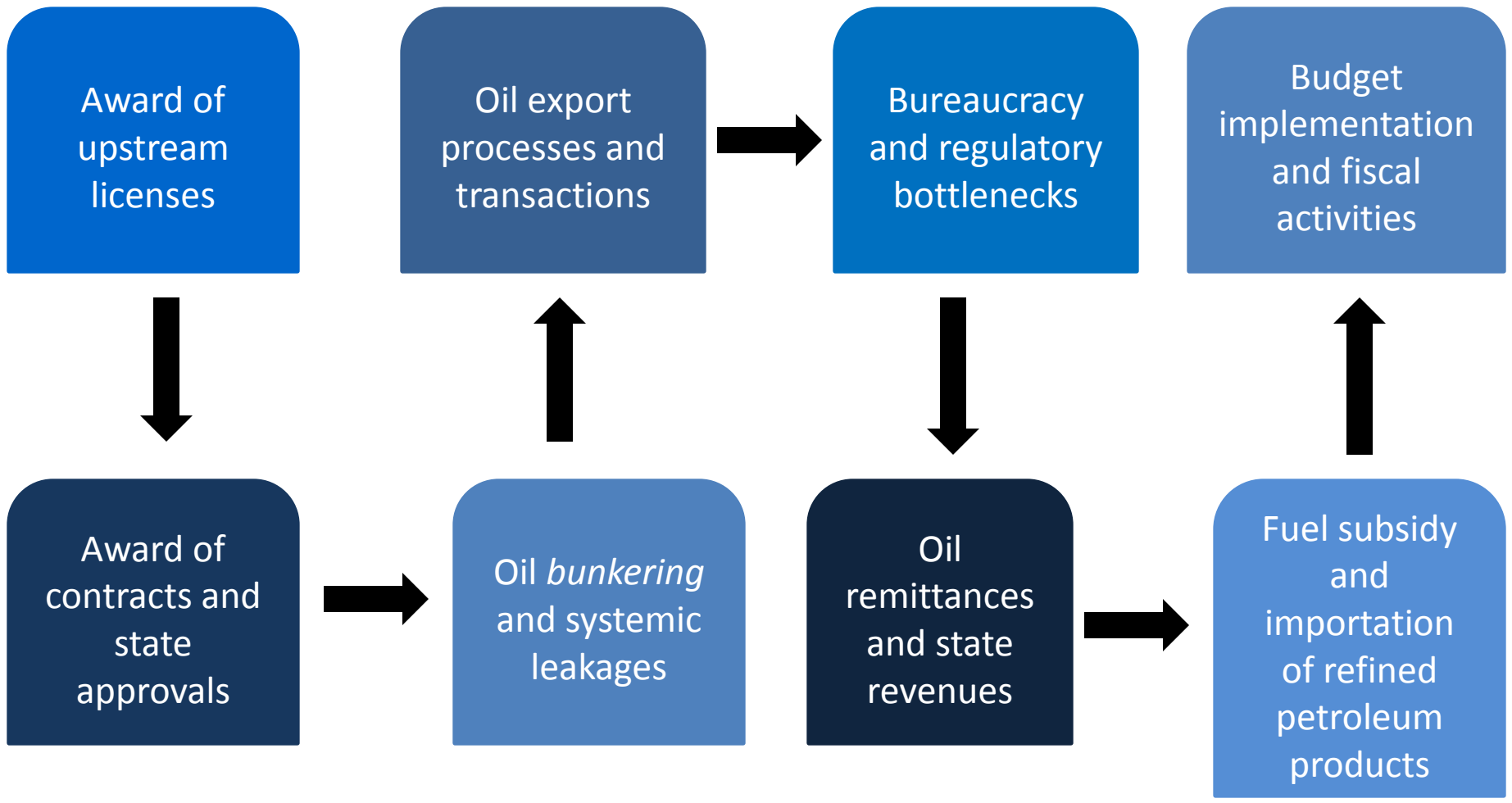
The Oil *Corruption Pipeline*

- Oil sector transparency in Nigeria can be understood using a sequential approach
 - What are the pressure-points at which corruption is concentrated?
 - Follow the ‘pipeline’: flow of oil rents in the economy
 - From the point where the oil licenses are granted, to operations, revenue remittances, fiscal allocations and policy implementation

‘The Extractive Industries Value Chain’



Following the *Pipeline*



Award of Upstream Oil Licenses

- Wide discretion over the award of oil exploration, production and mining licenses
 - Key state institutions include the Presidency, the Minister of the Petroleum and the regulator (DPR)
 - Introduction of competitive bidding rounds conducted by DPR (latest in 2007), still mired in controversy
 - ‘Briefcase companies’ often acquire upstream licenses in order to simply offload them to foreign oil companies and investors
 - This practice perverts the objectives of developing *local content*
 - Given the massive sums involved in upstream licensing transactions, oil blocks are extremely lucrative instruments of state patronage
- Need for open, transparent and participatory upstream licensing award process.

Award of Contracts and State Approvals

- Oil sector contracts must be approved by the NNPC (JV contracts over US\$ 1 million) and NAPIMS (PSC contracts over US\$250,000)
 - A lucrative source of state patronage as bribes are paid to secure contracts and approvals
 - Delays in reviewing contracts and excessive red tape further creates gatekeeper or *compradorial* roles for state bureaucrats and private middlemen
 - Contract tendering and operational approvals can also be used to secure financial gain for state officials and political leaders

Oil bunkering and systemic leakages

- Estimates of lost production due to oil bunkering range from between 100,000 to 685,000 bpd.
 - Up to 10% of Nigeria's international crude oil sales are believed to be in 'bunkered' or contraband oil
 - Bunkering reduces oil revenue due to the Nigerian state
 - Economic, (geo)political and security implications
 - Environmental damage and displacement of indigenous livelihoods in the Niger Delta
 - Fuels conflict , militancy and arms proliferation in the Niger Delta. Turf wars over lucrative bunkering routes.
 - Vast, sophisticated syndicates involving political actors, state and private oil company officials, armed youth groups and the security establishment implicated in bunkering

Oil export processes and transactions

- NNPC vested with the authority of granting oil export ('lifting') contracts.
 - NNPC enters into agreement with foreign and local oil companies for the production and export of crude oil. NNPC's partners sell their crude in international markets
 - Issues with the award of lifting contracts for NNPC's share of realised oil
 - Lack of transparency surrounding the process of awarding lifting contracts. Opaque guidelines for selection of contract holders
 - Furthermore, lack of information regarding the size and amount of lifting contracts
 - State officials and political leaders influence oil lifting contracts. In this way, the oil lifting contract is a strategic instrument of state patronage

Bureaucracy and regulatory bottlenecks

- Oil sector governance is hampered by a lack of transparency in the delivery of statutory responsibilities by strategic regulatory institutions
 - Fundamentally, conflation of regulatory and operational roles for the NNPC. NNPC's enormous influence on oil policy formulation and regulatory encroachment
 - Duplicative, conflicting roles for regulatory institutions
 - High political interference in routine regulatory operations
 - Low technical capacity to deliver statutory roles
 - Poor information disclosure, data management and inter-agency cooperation
 - Inadequate legal and legislative backing for sector regulation

Oil remittances and state revenues

- Lack of transparency surrounding basic information on revenues and receipts.
 - How much oil export revenues are earned by the Nigerian government; at what prevailing oil price?
 - Holding oil export receipts offshore is problematic. Legal? (outside Fed. Account); Transparent? (NNPC control)
 - Cost inflation and transfer pricing by foreign JV partners and tax/revenue implications
 - No independent checks and balances for transactions on the oil revenue accounts
 - Utilisation of saved oil revenues – management of the Excess Crude Account. Legal and oversight questions which the SWF should address.

Fuel Subsidy

- Low domestic refining capacity to meet energy demand results in importation of refined petroleum products
 - Private marketers import refined fuel at a market price (N140/litre, incl. import + landing costs), and sell to Nigerians at a subsidised price (N65/litre)
 - PPPRA reimburses the companies the difference between the subsidised and market price
 - Lack of transparency related to administration of the subsidy (e.g. award of import licenses, payments to fuel importers, subsidy financing and NNPC deductions)
 - Massive racketeering: e.g. Round tripping of locally refined products, false and inflated subsidy claims.
 - Broad consensus that the subsidy is in dire need of reform – N1.3 trillion spent on subsidy from Jan to Aug 2011, which exceeds capital expenditure (N1.1 trillion) in 2011!

The budget and fiscal activities

- How well does Nigeria utilise oil revenues?
 - Oil is the main source of government finances: Over three-quarters of Federation revenue derived from oil.
 - Efficiency in public expenditure: is oil revenue reaching the poor? Recurrent spending in 2011 is 74% of the total budget, while capital (development) spending is 26%.
 - Sub-national fiscal transparency: States rely on statutory allocations based on oil revenue, and account for 50% of consolidated spending, but little is known of their fiscal affairs
 - The Niger Delta crisis: Failure to lift the oil-producing communities out of poverty. Violence and conflict.
 - Paradox of plenty: Poverty and social inequality in the midst of enormous oil earnings (over US\$400 billion since 1960)

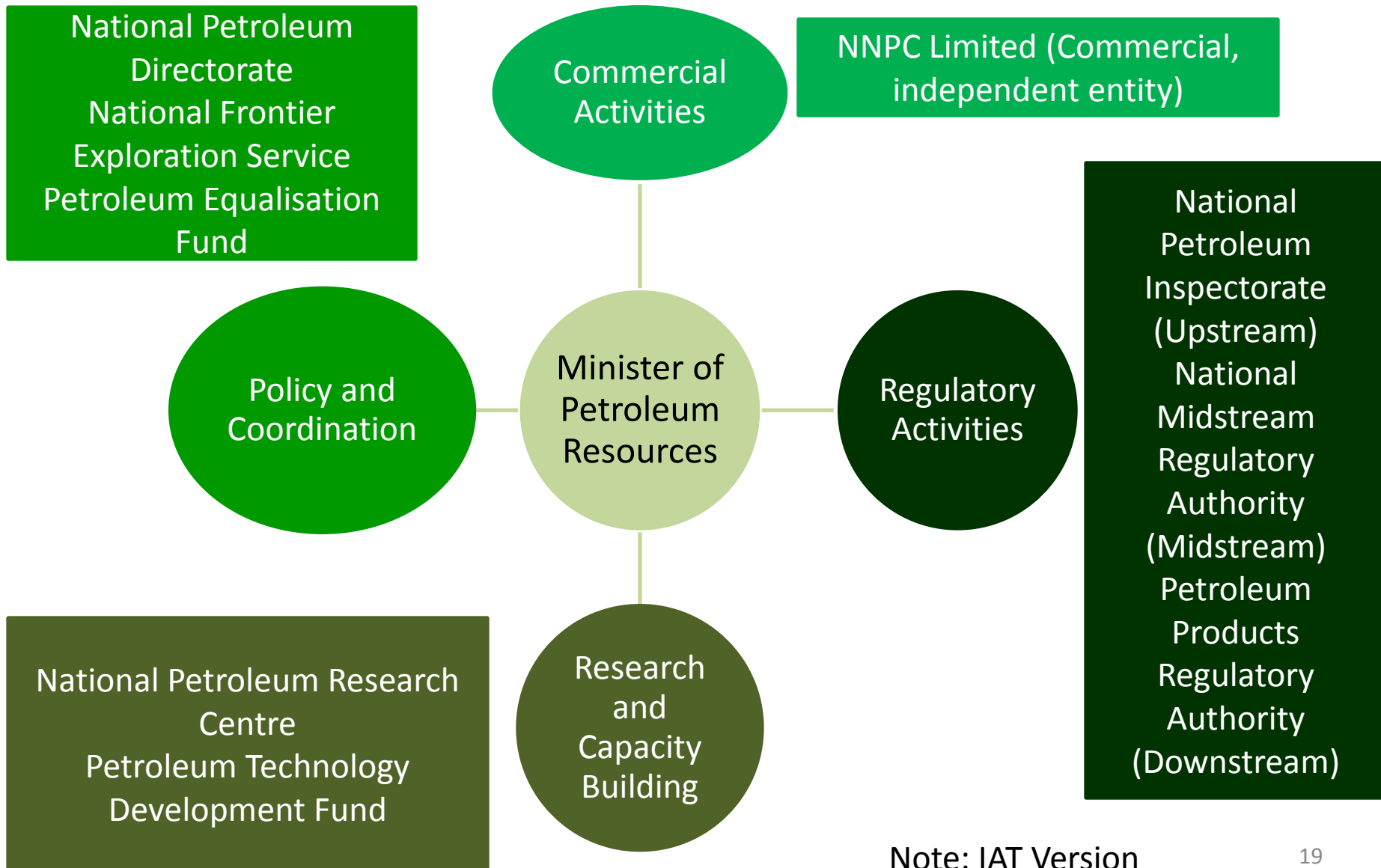
The PIB and oil sector governance

- The Petroleum Industry Bill is an ambitious attempt to overhaul the operational structure and governance of the Nigerian oil and gas sector
 - Three, well-known, competing versions - the original Presidency Bill (2008), Inter-Agency Team Memorandum (2010), and the Senate (combined) version (2011)
 - The policy debate should be structured around what the PIB can do to address the identified transparency issues
 - However, certain transparency gaps (such as budget implementation) require wider structural and institutional reforms
 - PIB is concerned with operational efficiency of the oil sector, and does not address oil revenue management (e.g. Angola, Ecuador)

The PIB and oil sector governance

- A fundamental change in the governance of the oil sector is the creation of nine (9) governing institutions by the PIB (based on the IAT version)
 - Four types of governance functions: commercial activities, policy and coordination, regulatory activities, and research and capacity building
 - Separation of regulatory and commercial activities – to reduce duplication of roles and inefficiency
 - Commercialisation of NNPC
 - However, there may still be a need to reduce the number of regulatory bodies
 - Wide, discretionary powers enjoyed by the Minister of Petroleum Resources

The PIB-proposed oil sector governance structure



Suggested Transparency Reforms

Upstream licenses: PIB should mandate open, transparent and participatory upstream licensing awards process

Oil export processes and transactions: PIB should introduce clear guidelines for award of oil lifting and midstream contracts.

Bureaucracy and regulatory bottlenecks: PIB should overhaul NNPC. Give clear regulatory roles. Mandate information disclosure. Compliance with NEITI and FOI Act.

The budget: Public expenditure tracking. Grassroots campaign on sub-national fiscal transparency. Political and institutional reform.

Award of contracts and state approvals: PIB should state clear guidelines for the award of contracts. Reduce red tape and approval delays

Oil bunkering: PIB should state guidelines for oil metering and calibration. Wider security and legal efforts to secure oil facilities. Address grievances of oil communities .

Oil revenue management: PIB should clearly state the 'chain of custody' for all oil revenue streams. Consistency with the SWF.

Fuel subsidy : PIB should state clear guidelines for import licenses. Radical subsidy reform.

The PIB and transparency reforms

- Complexity of oil activities and revenue flows requires us to look beyond the PIB to improve oil sector governance and transparency
 - As indicated above, the PIB is extensive, but still needs to be strengthened in order to be effective
 - Importance of complementary laws such as the NEITI Act, FOI Act and FR Act
 - The devil is in the details: Institutional capacities, statecraft, and political economy factors will determine the impact of oil transparency reforms
 - Important to link the PIB with the *Extractive Industries Value Chain*: oil operations should not be governed in isolation of oil revenue management

Discussion

- Specific transparency and governance provisions to strengthen the PIB
- Legal, constitutional framework for oil transparency reforms
- Integrating oil revenue management with transparency reforms
- Sub-national fiscal transparency – How can oil revenues impact grassroots communities?

Thank you