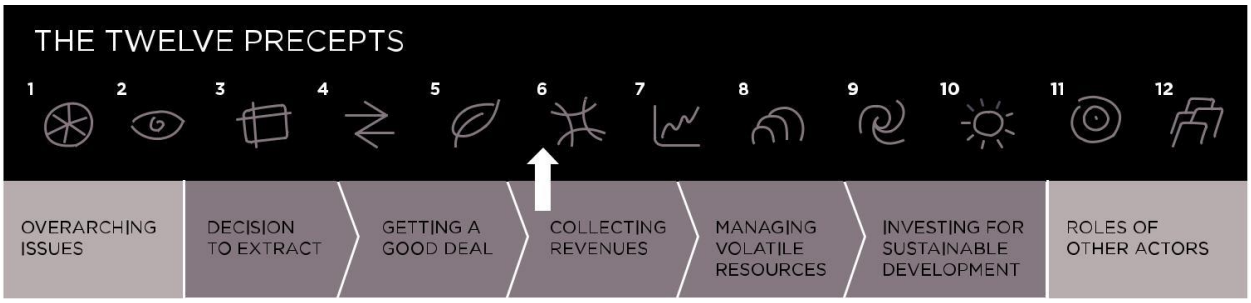
NIGERIA NATURAL RESOURCE CHARTER

2019 BENCHMARKING EXERCISE REPORT

PRECEPT 6: STATE OWNED ENTERPRISES: NNPC



Nationally owned companies should be accountable, with well-defined mandates and an objective of commercial efficiency.

Overall precept score	
Precept 6: SOEs Change in NNPC's leadership in the review period has not altered the Corporation's recent practice of disclosing selective unaudited operational and financial information. However, lack of legal provisions mandating such practices raise sustainability concerns. Furthermore, stalled petroleum industry reform in the 8th Assembly leaves several of the factors limiting NNPC's ability to operate transparently with the objective of being commercially viable in a competitive environment firmly in place.	⇧

Overview of the questions and ratings	
6.1 SOE ROLE AND FUNDING	
6.1.1 Does the government clearly define a commercial role for the NNPC that reflects the company's actual financial and technical capacity?	
6.1.2 Does the government clearly define the company's non-commercial roles? Does this definition limit conflicts of interest?	
6.1.3 Does the government ensure that the NNPC has a workable funding mechanism?	
6.2 SOE CORPORATE GOVERNANCE	
6.2.1 Does the government clearly establish the identity and role of state shareholders in the NNPC?	
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6.2.3 Does the NNPC invest in staff integrity and capacity?	
6.3 SOE TRANSPARENCY AND ACCOUNTABILITY	
6.3.1 Does the NNPC disclose key operational and payment data?	
6.3.2 Does the NNPC subject itself to independent financial audits and publish the results?	
6.3.3 Does the legislature oversee NNPC performance without unduly constraining its decision making?	

Summary of key findings

SOE role and funding

- An appraisal of the commercial performance of NNPC subsidiaries reveals that the discretion the Corporation enjoys in pursuing commercial interests, under current laws, limits its performance, thereby affecting its ability to generate returns for the country.
- NNPC dabbles into all spheres of the petroleum industry, specifically in operation, regulation, and policy by virtue of its position. This is likely to continuously lead to conflict of interest, lack of focus, inefficiencies and underperformance.

SOE corporate governance

- While the current corporate governance structure of NNPC, with strong Presidential influence, can allow for coherent strategic decision-making, it remains susceptible to excessive political interference and limits accountability through checks and balances.

SOE transparency and accountability

- NNPC continues the practice of disclosing selective unaudited operational and financial information in the review period. Yet, lack of underlying legal instruments to ensure sustainability of this practice and failure to enact necessary legislation to kick start petroleum industry reform constrains transparency and accountability in Nigeria's national oil company.

6.1 SOE role and funding

6.1.1 Does the government clearly define a commercial role for the NNPC that reflects the company's actual financial and technical capacity?

Old response: NO

New response: NO

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

The NNPC Act (1977) empowers the Corporation to “engage in all commercial activities relating to the petroleum industry”. NNPC in exercise of this provision has established several subsidiaries with interests along the entire value chain of the petroleum industry. However, the level of discretion NNPC has under the Act allows it to pursue interests in the petroleum industry that may not reflect the technical and financial capacity of the Corporation. For instance, consider the difference in commercial performance of NNPC subsidiaries (Figure 6.1). While the observed differences are partly due to operational challenges, perpetually poor performance in many subsidiaries reflect the deficiency in the definition of a clear commercial strategy. Such a strategy ought to be based on a well-considered outcome of a risk-reward calculus and an honest appraisal of the Corporation’s current financial and technical capacity.

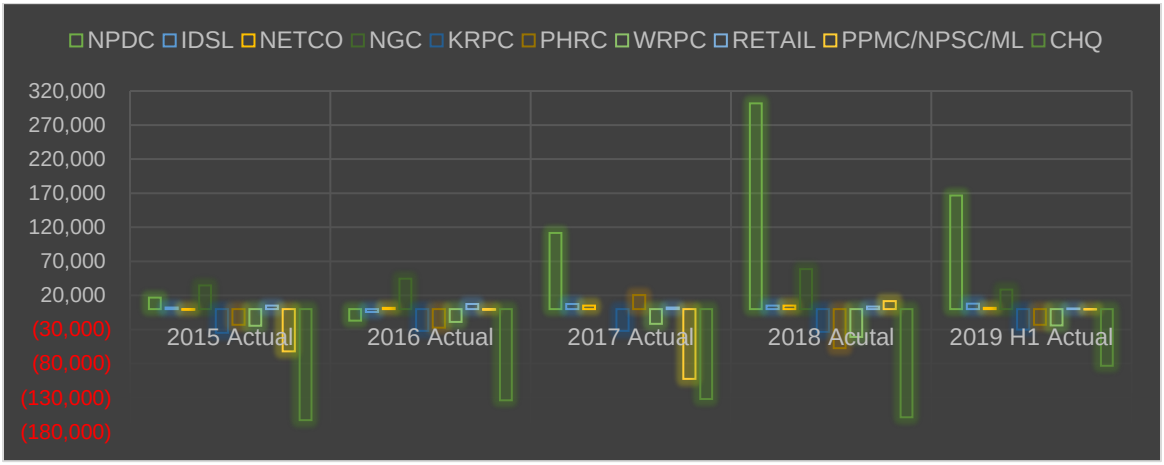
NNPC’s financial performance data reveals strong commercial performance for some subsidiaries like NPDC since 2017, whereas others such as refineries and ventures repeatedly return operational deficits (*Figure 6.1*). Moreover, the positive performance of the NPDC could have been more if well governed and unintended cross-subsidization with non-performing subsidiaries are checked and stopped.

A review of the subsidiaries grouped under ‘NNPC Ventures’ like NNPC Medical Services, which aims “to be the best healthcare provider in the country”, also reveals that the Corporation is pursuing commercial roles/interests outside the petroleum industry. Although there is no provision delineating activities that NNPC cannot carry out in the Act, its engagement in areas outside its core competencies may be driver for the poor performance observed in these areas. Moreover, branching outside of the petroleum industry may lead to waste in human and financial resources on a wide range of ill-suited activities that fail to generate returns for the country.

Furthermore, the Petroleum Industry Governance Bill (PIGB) passed by the 8th Assembly did not get Presidential assent, rolling back progress on reform efforts aimed at restructuring public entities and refining the definition of their roles in the petroleum industry. The Bill had proposed to establish two incorporated companies from NNPC, the Nigeria Petroleum Assets Management Company (NAPAMC) and the Nigerian Petroleum Company (NPC). Both entities were to be governed and managed based on the provisions of the Companies and Allied Matters Act (CAMA) and the Nigeria Securities and Exchange Commission (SEC)’s Code of Corporate Governance as opposed to the Public Procurement Act and other MDA regulations. Industry experts suggest

that uncertainty for investors due to the lingering industry reform costs the industry about US$15-20 billion in direct investments annually.

Figure 6.1: Selected NNPC Group Financial Performance by Entity (Surplus/Deficit)



Source: NNPC Monthly Financial and Operations Report

Information sources

KPMG. (2017). *The Petroleum Industry Governance Bill*. Retrieved from www.kpmg.com/ng

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NNPC Monthly Financial and Operational Reports. Available at https://www.nnpcgroup.com/

Olorunsola, Osten. (2018). *Without PIGB, FG Should Say Goodbye to ERGP*. Retrieved from: http://www.nigerianrc.org/olorunsola-without-pigb-fg-should-say-goodbye-to-ergp/

Olayinka, Collins & Daka, Terhemba. (2018). *Nigeria: Experts Insist Buhari Should Sign PIGB Into Law*. Retrieved from: https://allafrica.com/stories/201804220055.html

6.1.2 Does the government clearly define the company's non-commercial roles? Does this definition limit conflicts of interest?

Old response: NO

New response: NO

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

NNPC's unique positioning in the Nigerian petroleum industry allows it to play roles in all spheres of the industry, specifically in operations as noted above, regulation, and policy.

The NNPC Act (1977) empowers the Corporation to "enforce all regulatory measures relating to the general control of the Petroleum sector through its Petroleum Inspectorate department." However, the Petroleum Inspectorate moved to the Ministry of Petroleum Resources in 1988, eventually morphing into the entity now referred to as the Department of Petroleum Resources (DPR). Irrespective of the current arrangement, regulatory provisions remain in the Act and NNPC continues to have significant influence on regulation in the industry. Specifically, we see NNPC making regulatory and policy pronouncements, and this creates significant institutional recklessness, perennial conflicts and/or an undue advantage for the Corporation as an operator. In fact, NNPC operates as if above being regulated, making it very difficult to carry out their roles as they do across the industry.

Although the NNPC Act does not explicitly provide for policy functions for the Corporation, NNPC's superior technical capacity (human resource) relative to the Ministry of Petroleum Resources (MPR) allows it to influence policy. Particularly, the Minister for Petroleum Resources always sees the NNPC as ready backroom policy support to the disrespect to the core staff of the Ministry. Successive Ministers tend to rely on NNPC's human resources due to the deficiencies in the MPR given the civil service structure with features such as transfers that limit sector-specific expertise relevant for policymaking. Moreover, the NNPC Towers houses the MPR and current legal provisions make the Minister of Petroleum Resources NNPC's board chair.

Furthermore, NNPC takes up socio-political and quasi-fiscal activities such as ensuring regular supply of PMS nationwide, irrespective of the market forces. The Corporation maintains monopoly of supply and regulates the price by absorbing the difference between that price and the cost of importing the product. Being the sole importer of PMS, NNPC takes on the financial responsibility of any differences between the supply costs and retail prices in form of price recovery. This has significant implications on NNPC's books and its remittances to the Federation Account. In addition, the good principle of check and balance is completely non-existent, thus entrenching suspicion of the citizenry.

The PIGB that was passed by the 8th Assembly, sought to delineate roles for specific new public entities to improve the governance in the petroleum industry. Particularly, it provided for the creation of the National Petroleum Regulatory Commission (NPRC) as the sole regulator for the petroleum industry. Until the government implements such reforms, the current influence of NNPC across the different spheres of industry practice will persist.

Information sources

Nigerian National Petroleum Corporation Act. (1990).

Stakeholder Engagements

6.1.3 Does the government ensure that NNPC has a workable funding mechanism?

Old response: NO

New response: PARTIALLY YES

UPDATE STATUS: SOME CHANGES OBSERVED

Previously, NNPC relied on allocations from the federal government budget to fund its cash call obligations. The NNPC Act mandates the Corporation's expenditure to follow the appropriation process. Under this arrangement, NNPC struggled to meet its funding obligations in quantum and in a timely manner. More recently, NNPC has taken steps to adopt a more workable funding arrangement, especially for equity contributions on joint ventures.

In the period under review, the cash call budget previously approved along with the federal annual budget is no longer funded directly by the federal government. Instead, NNPC relies on aggregate revenues from its subsidiaries and business units, deductions from oil revenue due to the Federation, and third-party financing for approved projects to finance its operations.

Furthermore, immediate past NNPC GMD, Maikanti Baru, expressed a renewed desire to introduce incorporated joint ventures (IJVs) in order to help finance investment needs through debt. Such an arrangement could have significant implications for government revenues, transparency, and partnership arrangements with operators. For instance, NNPC will receive a share of IJV revenues after expenses and taxes as dividends instead of direct proceeds of sales. While the idea of IJVs has been floated since 2008, there has been concerns that constrained its adoption. Particularly, in previous iterations of the petroleum industry bills, there were concerns around the proposed shareholding structure where government was to maintain controlling shares amid fears of the likelihood of undue political interference.

Information sources

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Two Options for Converting NPDC's Unincorporated Joint Ventures to Incorporated Joint Ventures. (2015). Retrieved from: http://www.petroleumindustrybill.com/tag/incorporated-joint-ventures/#.XaQ14UZKi00

6.2 SOE corporate governance

6.2.1 Does the government clearly establish the identity and role of state shareholders in the NNPC?

Old response: YES

New response: PARTIALLY YES

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

The Nigerian government fully owns NNPC, a statutory corporation charged with the responsibility of representing the Federation's interest in the petroleum industry. The federal government is responsible for strategic decision-making regarding NNPC such as management and board appointments. In practice, the President makes the key decisions often influenced by the Minister of State for Petroleum Resources when there is one. During the review period, a Federal High Court delivered judgement on a suit that challenged the President's ability to hold the position of Minister of Petroleum Resources. The court held that such practice was not in violation of the law given that someone else oversees the day-to-day running of the ministry, which at the time was Ibe Kachikwu.

Under the current arrangement, the decision-making is vested in a strong single state actor –the President, which allows for coherent strategic choices. It, however, encourages undue political interference and limits checks and balances. Enhanced but clearly defined roles for other state shareholders beyond the President may improve accountability through useful checks and balances.

Following from the legislative process that led to the passage of the PIGB, the current consensus position on reform regarding ownership of NNPC is to restructure the Corporation to create the National Petroleum Company (NPC) in addition to the Nigerian Petroleum Liability Management Company, Nigerian Petroleum Assets Management Company Limited. While the government will maintain majority shareholding in NPC, there is allowance for public ownership of a limited shareholding in the Company.

Information sources

Olisa Agbakoba Legal. (2018). Retrieved from: http://www.mondaq.com/Nigeria/x/757892/Constitutional+Administrative+Law/Federal+High+Court+Holds+that+Buhari+Cannot+be+President+and+Minister+of+Petroleum

Petroleum Industry and Governance Bill. (2018). Retrieved from: http://www.petroleumindustrybill.com/wp-content/uploads/2018/04/Harmonised-Clean-Copy-of-Petroleum-Industry-and-Governance-Bill-2018.pdf

Stakeholder Engagements.

6.2.2 Does the NNPC have an empowered, professional, and independent board?

Old response: NO

New response: NO

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

Provisions for constituting the NNPC Board are stipulated in the NNPC Act, which provides for the Minister of Petroleum Resources (MoPR) to act as Chairman of the Board. It also provides for a representative of the Ministry of Finance but little room for executive directors, with only the GMD of NNPC represented on the Board. While the Act allows for private sector participation, there is no representation of private actors on the current NNPC Board. Consequently, the set-up of the Board by design and practice make for heavily government-oriented Board, also reflecting the ownership structure.

Little wonder the set-up described above freely allows for political interference. The minister, who is responsible for policy in the industry, being Chairperson of the board, may be driven by policy considerations at best and political considerations at worse. While the current constitution of the does not violate the Act, NNPC corporate governance might improve if board members are largely independent and selected based on technical capacity and competence. This can be done by recruiting board members from outside the government to bring the right skills needed for effective decision-making.

Information sources

Nigerian National Petroleum Corporation Act. (1990).

Stakeholder Engagements.

6.2.3 Does the NNPC invest in staff integrity and capacity?

Old response: PARTIALLY YES

New response: PARTIALLY YES

UPDATE STATUS: NO OBSERVABLE CHANGES

Improving the competence of staff through training and providing incentives can safeguard against narrow rent seeking and promote overall organizational effectiveness. The NNPC has one of the more robust remunerations and professional development structures among Nigerian public service organizations. The NNPC's Leadership Academy was established to provide technical, managerial and executive training within and outside the corporation. In the past, the corporation has publicized its staff anti-fraud training activities. However, it is not clear that the corporations' investment in staff capacity translates into staff integrity. This is even as recruitment into the corporation as well as appointments to key positions still appears to be subjected to political patronage, socio-ethnic and religious considerations. In addition, some laws and

regulations require equal staffing considerations from all 36 States of the Federation which can impede the selection of the best and the brightest for advancement.

Information sources

NNPC Leadership Academy (NLA). (n.d.). Retrieved from: https://www.nnpcgroup.com/Ventures/Pages/NNPCLeadershipAcademy.aspx

6.3 SOE transparency and accountability

6.3.1 Does the NNPC disclose key operational and payment data?

Old response: NO

New response: PARTIALLY YES

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

NNPC has maintained the practice of disclosing selective and unaudited monthly operational and financial performance data since 2016. Despite the disclosure of information by NNPC in recent times, it is important to examine the implications and unintended consequences of increased information disclosure. Specifically, shining light on some information may conceal other issues in darkness.

Furthermore, transparency or information disclosure is not an end in itself. It is instrumental for seeking accountability. Too much emphasis on information disclosure is misplaced, especially when the assumption that the availability of information incentivizes good behaviour among decision makers fails. The information disclosed has to be useful and civil society and the public have to be able to understand and use it. In this regard, the timeliness, understanding and faithful representation of the data are important. While transparency can point to wrongdoing and identify who should be held accountable, it is redundant in many cases where other accountability infrastructure subverts its impact.

In addition, the disclosure of operational and financial information by NNPC since 2016 has banked on the preferences of the leadership at the Corporation. The fact that this transparency measure remains under the purview of personal initiative and not under legal requirements raises institutional and sustainability concerns.

Information sources

Abdul-Baki, Z. (2019), "The role of accounting in conflicts resolution", *Managerial Auditing Journal*, Vol. ahead-of-print No. ahead-of-print. https://doi.org/10.1108/MAJ-03-2018-1835

Ejiogu, A., Ejiogu, C., & Ambituuni, A. (2018). *The dark side of transparency: Does the Nigeria extractive industries transparency initiative help or hinder accountability and corruption control? The British Accounting Review.* doi:10.1016/j.bar.2018.10.004

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NNPC. (n.d.). *NNPC Monthly Performance Data (several months)*. Retrieved from https://www.nnpcgroup.com/NNPC-Business/Business-Information/Pages/Monthly-Performance-Data.aspx

6.3.2 Does the NNPC subject itself to independent financial audits and publish the results?

Old response: PARTIALLY YES

New response: NO

UPDATE STATUS: ADDITIONAL INFORMATION INCLUDED

The law (Section 7 subsection 2-3 of the NNPC Act, 1997) mandates NNPC to conduct regular audits of its operations using independent auditors. Available evidence suggests that in the past, the Corporation has only subjected itself to these audits at the behest of the federal government; including its only publicly available 2015 audit to investigate allegations of unremitted funds into the federation accounts by the Corporation. Meanwhile, as part of its drive towards more transparency, in 2018, the Corporation announced the completion of its group financial audit for five years between 2011 and 2016. Although NNPC has made a concerted effort to make public monthly financial and operation reports, its audit report(s) are however not publicly available.

The lack of a culture of openness and disclosure within the system is partly responsible for the poor record keeping, lack of check and balance, ineffective performance reviews and audits, as well as absence of transparency and accountability in NNPC. Historically, the government does not seem to value transparency and has not meaningfully sought same from NNPC or investigated wrongdoings in a way that leads to consequences and penalties on one hand, as well as positively capturing learnings for institutional improvement the future. This extremely weak transparency and accountability culture means that staff, as well as decision makers are not incentivized to be transparent.

Furthermore, anecdotal evidence from a 2016 audit of the Federal government's books (published in 2018) suggests that huge amounts of generated revenues were unremitted by NNPC to the federation account, and its crude oil exploration and operations records were opaque.

Information sources

Daily Trust Newspaper. (2018, May 18). *KPMG Audit Shows NNPC, Others Failed To Remit N8trn Between 2010 And 2015 | Sahara Reporters*. Retrieved from: http://saharareporters.com/2018/05/18/kpmg-audit-shows-nnpc-others-failed-remit-n8trn-between-2010-and-2015

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Okechukwu Nnodim. (2018, April 9). *NNPC completes group financial audit for five years – Punch Newspapers*. Retrieved from: https://punchng.com/nnpc-completes-group-financial-audit-for-five-years/

6.3.3 Does the legislature oversee NNPC performance without unduly constraining its decision making?

Old response: NO

New response: NO

UPDATE STATUS: ADDITIONAL INFORMATION ADDED

Primarily, Nigeria's legislature maintains oversight over the NNPC through its constitutional powers to enact laws and approve the budgets of government agencies. In the past, NNPC's cash call funding followed the legislative appropriation process, which is susceptible to delay and politicking. More recently, NNPC funding has not appeared in the budget of the federal government given the different funding arrangement it now employs for JVs.

Furthermore, the legislature often plays a reactive role to oversight, by mainly constituting inquiries into alleged wrongdoings by NNPC. In the review period, legislative efforts have not led to NNPC leaders facing punitive consequences for wrongdoing or poor performance. For instance, probes initiated by the National Assembly such as investigating alleged diversion of funds for subsidy payment and non-remittance of funds to the Federation Account have not led to legal consequences for NNPC. However, the National Assembly's probe of NNPC's under remittance of funds to the Federation account stirred conversations and may have partly influenced more disclosures by the Corporation.

To avoid unduly constraining NNPC decision-making, legislative oversight can be limited to fixing problems with the legal or legislative framework governing the petroleum industry generally and NNPC particularly. Issues of corporate governance are often under the purview of corporate boards; therefore, legislative overreach in such areas may constrain the Corporation's decision-making and efficiency.

A more proactive approach to legislation will be enacting laws that address loopholes and improve institutional governance in the petroleum industry, as well as improve NNPC's corporate governance structure. Unfortunately, such efforts through the PIGB for instance have been a subject of politics and controversy and have still not led to substantive legislation.

Information sources

Emmanuel Abara Benson. (2018, October 17). *NNPC under fire as Senate inaugurates fresh oil subsidy investigation*. Retrieved from: https://nairametrics.com/2018/10/17/national-assembly-opens-fresh-subsidy-investigation/

Leke Baiyewu. (2018, October 14). *Reps summon ministers, NNPC boss over illegal subsidy payments – Punch Newspapers*. Retrieved from: https://punchng.com/reps-summon-ministers-nnpc-boss-over-illegal-subsidy-payments/

Stakeholder Engagements.