



**MEMORANDUM SUBMITTED
TO THE
SENATE COMMITTEE ON FINANCE
ON THE
NON-REMITANCE OF OIL REVENUE TO THE
FEDERATION ACCOUNT**

BY

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Mr. Chairman,

I write to provide an update on the above subject after going through the interim report submitted to me by the technical team in the Central Bank of Nigeria (CBN) and other reports. Mr. Chairman, you will recall that this investigative hearing started as a result of a letter I wrote to the President in September, 2013, requesting for an investigation into a report I received indicating a difference of almost \$50 billion between the value of crude oil lifted by the NNPC (\$65 billion) and the amount repatriated into the Federation Account (\$15 billion) in the period, January, 2012 to July, 2013.

In December, 2013, we had appeared before this Committee and indicated that reconciliation was on-going. Since then, Senior Officials of NNPC have made public statements on the pages of newspapers and national television explaining what they had accepted was a shortfall of \$10.8 billion.

I have taken time to review the various submissions of the NNPC at the reconciliation meeting, the various explanations given to the public, documents available to me from the Central Bank of Nigeria and other sources and advice obtained over time from professionals. My presentation today supersedes my earlier submission of December and represents the result of my own detailed examination into the subject.

Background

Mr. Chairman, the interest of the Central Bank of Nigeria in the revenue profile of the country has been a long-standing one. As far back as 2010, the CBN had been raising alarm over the clear anomaly of the country's reserves not rising in the wake of strong recovery in Oil prices. At that time I recall that I went to NNPC with my entire Committee of Governors to ask the Management for an explanation. We were told that the basic issue was that most of our Oil production was coming from deep off-shore wells under Production Sharing Contracts, where the Government take was less than under Joint Ventures (JVs). We were further informed that the fiscal terms of the PSCs were defined at a time when the price of Oil was \$10 per barrel, and fixed for 30 years by the military administration of General Abacha.

Further, the impression we had was that these terms could not be revised in favour of the country without passage of the PIB.

Mr. Chairman, after the 2010 meeting, I came to discover that a PIB is not necessary for a re-negotiation of the fiscal terms of the PSCs. I have attached (as Appendix 1), a legal opinion recently updated on this matter from AB Mahmoud, a Senior Advocate of Nigeria (SAN) with Dikko and Mahmoud. But I will not spend too much time on this.

The important issue is that once this was made clear to me, I and my colleagues shifted our focus to what may be revenue leakages in the system. In late 2010, at a Public Hearing in the House of Representatives, I raised an alarm over what I suspected was a huge racket around the payment of petroleum subsidy claims. This was long before the various investigative panels around fuel subsidy were set up. At that time, after my presentation at the House, I received a protest letter from PPPRA seeking to educate me on the subsidy payment process and providing some useful information. I attached that letter here (as Appendix 2).

Subsequent investigations by several Committees, including the House of Representatives Committee and the Aig-Imoukhuede Committee established that my concerns were genuine and that indeed there was a huge fraud taking place in the fuel subsidy regime, even though no serious action seems to have been taken up to this point. During the House of Representatives investigation, I submitted a detailed letter summarizing, again, my presentation of 2010 and outlining exactly how the subsidy fraud was carried out. I attach that letter here (as Appendix 3).

We also turned our attention to leakages from the system through opaque and complex Swap transactions between PPMC and some counter-parties. By 2011 it was already clear to us that these transactions were not properly structured, monitored and audited. For example, companies in Swap agreements with PPMC would lift Crude Oil for free, sell at the international market, repatriate the funds and sell at the autonomous rate, trade with the proceeds and at their own time establish letters of Credit (LCs) to import PMS using funds purchased at the official window. At this point, we limited our intervention to what we could control, and

issued a Circular banning these companies from accessing wDAS for their imports. I attached the circular here (as Appendix 5).

Mr. Chairman, I will not go into details on my concerns around Swap transactions. I am attaching, (as Appendix 6), a guidance note I prepared with advice from an expert in the area. I am aware that the National Assembly is investigating these Swaps at the moment. The note gives a good idea of areas to scrutinize, and I am also providing three Swap Contracts to assist in the analysis. These were contracts signed between NNPC and the Societe Ivoirienne de Raffinage (SIR), (See Appendix 7) between PPMC and Duke Oil Services, (see Appendix 8) and between Duke Oil Services and Taleveras Petroleum Trading BV. (See Appendix 9). As indicated in my guidance note, however, I do not believe this particular investigation will yield any results. The Agreements signed by PPMC contained a troubling clause that permits destruction of documents after one year. (See Article 12 of Appendix 8 and Article 18 in Appendix 7). My note in Appendix 4 identifies possible areas of loss of revenue to include Terms of Sale, Unjustified use of Intermediaries, verification of "equivalent value" and importation and transportation of products.

Mr. Chairman, I have gone into these details to make a simple point. My engagement with the subject did not commence in 2013 with my letter to the President. It has been a constant theme of my term as Governor of CBN, because the failure of NNPC to remit foreign exchange to the Federation Account in a period of rising Oil prices has made our management of exchange rates and price stability, while keeping reserve buffers adequate, extremely difficult. The economy has had to pay a high price in very high interest rates and tight monetary conditions.

The Central Bank of Nigeria is always blamed for high rates of interest as most non-economists do not realize that, given these leakages, the alternative is a devalued currency, low reserves level, high inflation and financial instability.

Before I wrote my letter to the President in September, 2013, there had been several allegations against NNPC for non-remittance of funds to the Federation Account. NEITI had raised this issue in its various reports. The KPMG audit ordered by Minister Aganga, when he was in the Finance Ministry had raised the same issues.

The Nuhu Ribadu Committee set up by Petroleum Minister Allison-Madueke also made the same claims. It is also a regular subject of dispute between NNPC and FAAC.

Apart from the controversy that follows these allegations, nothing has happened, or changed. NNPC dismisses all such allegations as false and spurious, and claims in fact that the Federation owes it money. In a sense, we have made progress since NNPC has now for the first time acknowledged that it did not remit to the Federation a sum of \$10.8 billion and has gone public with an attempt to render account.

In my presentation today, Mr. Chairman, I will show that:

1. The amount of money illegally and unconstitutionally withheld, diverted or spent by NNPC is in excess of the \$10.8 billion, and
2. Provide documents showing exactly how this money was taken from the Federation.

In the rest of my letter, I will cover the following areas

- a. NNPC's response to my allegations
 - b. Analysis of NNPC claim on subsidy
 - c. Analysis of NNPC claim on Oil lifted by NPDC and
3. **Domestic Crude Sales Reconciliation**

Mr. Chairman, in order to avoid rehashing the explanation given by NNPC in December, please find attached (as Appendix 19) the presentation of NNPC at the technical reconciliation meeting. In summary, NNPC gave the following account of its crude oil lifting:

Total lifting	\$67 billion
Made up of	
1. Federation	\$14 billion
2. FIRS	\$15 billion
3. DPR	\$2 billion
4. NPDC	\$2 billion

5. Domestic Crude	\$28 billion
6. Third party financing	\$2 billion
Total	<u>\$67 billion</u>

I am satisfied that NNPC has sufficiently established items 1 – 3 as having been remitted. Items 2 & 3 represent crude NNPC lifted in its own name but which belonged to FIRS & DPR. The proceeds came into the CBN in the names of the IOC's paying PPT and Royalty, not NNPC.

I will show later why at least part of the \$6b lifted for NPDC should be considered Federation Account money, as it was money diverted to private hands unconstitutionally.

Domestic crude is paid into the Federation Account in Naira. We have attached, (as Appendix 20), all the monthly payments into this account and converted same into US Dollars. The total remittances amount to about \$16b out of the \$28b lifted by NNPC, leaving a shortfall of \$12b. This was number I gave at the December hearing.

Our records show that in the first Quarter of 2012, NNPC sent in FAAC returns indicating it had deducted N180b as subsidy on petroleum products imported by it. NNPC had been directed to stop subsidy deductions with effect from 2011. The management explained that these were deduction with respect to the imports in the last quarter of 2011. We attach the returns of NNPC for Q1 2012 and confirm that after March, 2012 NNPC did not send a single return indicating subsidy deductions.

We believe these deductions in Q1:2012 account for the difference between our \$12b and the \$10.8b of the Ministry of Finance. \$12b was the shortfall in remittance from domestic crude sales between January, 2012 and July 2013. N180b (= \$1.2b @ N150:\$1) was amount withheld by NNPC and disclosed to FAAC as subsidy for Q4:2011 imports. The \$10.8b therefore has taken this amount withheld into account, if PPPRA confirms that the N180 b claim is valid, we will accept it. We will now turn to the accounting for the \$10.8b.

The reconciliation team has not met since our last appearance before this committee. Fortunately, the NNPC was generous enough to issue a series of Press Statements and hold a series of press interactions explaining exactly how it spent the \$10.8billion. I plan to respond to these explanations and show why they are untenable.

On January 14, the GED of NNPC, Mr. Bernard Otti gave an explanation for how NNPC has spent \$10.8b. He said \$8.49b was spent on "subsidy claims" within the period, \$1.22b on management and repairs of pipelines, \$0.72b on crude oil losses NS \$0.37b on holding strategic products reserves. I have attached this (as Appendix 22).

The GMD of NNPC Mr. Andrew Yakubu reinforced this position on January 20, when he declared that about 80% of the \$10.8b was incurred on petrol and kerosene subsidy. He further declared that NNPC imports kerosene at a cost of over N150/litre and sells at less than N50/litre. (Appendix 23). The GMD did not give an indication of how much of the subsidy was for PMS and how much for kerosene, but we know from the Hon. Farouk Lawan committee report that NNPC, in 2011, processed payment of N310.4b as 2009-2011 arrears of subsidy on kerosene. Assuming this is the total it processed, this would suggest a rate of over N100b per annum on kerosene subsidy alone! I will begin therefore with kerosene.

Mr. Chairman, I refer you to three documents emanating from the office of the Principal Secretary to President Umaru Musa Yar'Adua, labeled Appendix 24 (a-c). 24(a) is a memo, with the written approval of the President, authorizing the communication of decisions taken at a meeting held on 9 June, 2009 with President Yar'Adua, Vice-President Jonathan, several Ministers (Finance, Transport, Petroleum) and the GMD of NNPC in attendance. The relevant directive to the Ministers of Petroleum was one **stating clearly that existing subsidy on the consumption of kerosene be eliminated "taking into account that subsidy payments by Government on kerosene do not reach the intended beneficiaries.** Appendix 24 (b) is a letter dated 17th June, 2009 to the petroleum Minister, formally communicating the decision of the President to implement w.e.f. July, 2009. On 19th October, the PSP send a letter to the National Security Adviser in which he confirmed from his registry that **the directives were received and acknowledged in**

the offices of the **Ministers of Petroleum and the GMD of NNPC**. So there is no question that this directive was received.

I also attach again (as Appendix 25) the letter to me from the Executive Secretary of PPPRA in December 16, 2010. In that letter, he confirmed that PPPRA had "ceased to grant subsidy on HHK through a presidential directive since July, 2009" what this shows is that

1. All parties concerned had received the presidential directive and
2. That this directive was still in force as at December, 2010, seven months after the death of 'Yar Adua.

This may explain why NNPC waited till 2011 to claim its "arrears" for 2009-2011. So the first question here is: on what basis did NNPC pay itself billions of dollars as "subsidy" for kerosene, in view of this directive. NNPC needs to provide us with evidence of its authority to pay.

Second, Mr. Chairman, it is clear from all the documents in Appendix 24 that the basis for the directive to eliminate subsidy was straight forward and unambiguous: there was no subsidy, as Nigerians were nowhere purchasing kerosene at the subsidized rate. The Federal Government recognized that kerosene subsidy was "economic rent", a racket in which NNPC bought kerosene at N150/litre, sold to marketers at N40/litre knowing well that the retail price was more in the region of N170 – N250 litre. The margin of 300% - 500% over purchase price is economic rent, which never got to the man on the street. In dollar terms, every vessel of kerosene imported by NNPC with Federation money cost about \$30m and it was sold for \$10m or \$11m, generating rent of \$20m/vessel to the syndicate.

Mr. Chairman, I attach (as Appendix 26) detailed tables from data issued by the National Bureau of Statistics (NBS) showing the price of Kerosene in every state of the country and FCT in 2012 and 2013. It also breaks this into Urban and Rural areas and provides the range of prices. The tables are self-explanatory. Kerosene is simply not a subsidized product anywhere in the country. I also attach (as Appendix 27) a letter from B. J. Rewane of Financial Derivatives Company Limited (FDC) attaching Kerosene prices in the Lagos area as well as a graph showing the value of economic rent being extracted in the kerosene business. Nigerian Port Authority

(NPA) records will show that NNPC imports about 4 – 6 vessels of Kerosene monthly. If we assume an average of 5 vessels a month and a “subsidy” of \$20m/vessel, NNPC has been unilaterally generating rent for itself and players in the Kerosene business at the rate of \$100m every month for a number of years. This entire amount represents a direct loss to the Federation Account. So we now have 3 issues:

1. Non-remittance of proceeds to FAC
2. Violation of a Presidential directive and
3. Paying subsidy on a product that is not subsidized

But even the claims on PMS subsidy are bogus and unsubstantiated. Please consider Appendix 28. This document lists out the monthly deductions from Domestic Crude Sales that NNPC made before remittance to FAAC IN 2009 – 2013. This table is based on monthly letters written by NNPC to CBN and disclosure commenced in October, 2009, (we are told) only after the National Assembly insisted on this happening.

The interesting point here is that NNPC from April, 2012 onward has consistently rendered a NIL return for subsidy deduction after reporting deductions for 30 consecutive months. NNPC has always said it stopped deductions after December, 2011 in compliance with the directives to submit its claims to PPPRA in line with the Law.

Also attach as Appendix 29 is the monthly CBN Federation Account component statement for 2012. It is evident that after March 2012, the row showing “adjustment for subsidy” was consistently showing a NIL return. We can on demand produce the statement for preceding and subsequent periods. This is proof that NNPC has consistently claimed it was making no deductions for subsidy after March 2012. So how did then \$8.49b subsidy explanation come about?

If NNPC was deducting fuel subsidy after March 2012, why did it deliberately render false returns and deny these deductions for so long? If the returns sent were true and there were no deductions, why is NNPC management making false public statements to Nigerians? NNPC management either made false representations to FAC for 20 consecutive months (April 2012 – Dec 2013) or else in issuing false

statements. Either way this shows we cannot trust NNPC or its management to tell us the truth.

Mr. Chairman, this brings me to the core of this issue. In the period 2006 to 2008 when oil price was at a historical peak, actual expenditure on subsidy for both PMS & HHK was N261.1b (2006), N278.8b (2007) N346.7b (2008). By 2011, NNPC alone deducted, unilaterally, N843b as subsidy, in addition to N848b it withdrew from the excess crude naira account. According to the Farrouk Lawan Committee, therefore, NNPC paid itself N1.7trillion as subsidy on PMS in 2011 alone. (See Appendix 29).

Going back to our 19 – month period, I would advise the committee to obtain from PPPRA details of the total claims made by NNPC in the period, as well as what percentage (by number value) if there claims were accompanied by evidence and paid. Also PPPRA should indicate the date on which these claims were filed. If NNPC was not filing the claims regularly, why not?

In any event, let us analyse NNPC's claims. NNPC says it paid \$8.49b as kerosene and PMs Subsidy. Based on our earlier analysis let us assume HHK "subsidy" at \$100m/month. This means about \$1.9b out of this amount was HHK and about \$6.6b was PMS. Converting at N160 gives N1.056trillion. When we add the N180b declared in Q1:2012 gives total of N1.236 trillion over 19 months.

Now, let us assume fuel subsidy at N44/litre in line with PPPRA template. Let us also assume average vessel size of 30,000 MT and approximately 1,136 litres in a metric ton. This brings the subsidy per vessel to about N1.5b. If NNPC is claiming it paid N1.236 trillion as subsidy on PMS in this period and \$1.9b as subsidy on kerosene, then it imported 95 vessels of HHK and about 825 vessels of PMS (at 30,000 MT each) in the period. NNPC should produce data on these 825 vessels and proof of inspection and discharge.

Further, if the numbers in Appendix 29 are correct, NNPC in 2011 alone collected about N1.7trillion as subsidy on PMS in addition to over N300b as "subsidy arrears" on HHK. I have not independently verified all these numbers. But if NNPC did collect so much in 2011, NNPC's data base needs to be independently audited with

claims checked against NPA and international shipping records to ensure that these claims are legitimate. As a rule of thumb, every \$1b claimed as subsidy should be accompanied with proof of importing at least 100 vessels of 30, 000MT each.

NPDC

In the explanation offered by NNPC, its Management also indicated that it lifted crude worth \$6b on behalf of NPDC. I intend to argue that a substantial amount, out of this, constitutionally belongs to the Federation Account, as the crude being exported by NPDC and its business partners is partly from Oil blocks belonging to the Federation and managed in trust by NNPC. NNPC, took away blocks from the Federation and gave them to itself (using NPDC as an SPV) and then transferred the operation of the blocks to agents with limited experience in operating oil blocks. These agents used the blocks to raise finance, produce oil, sell and keep the proceeds, sharing these with NPDC. Let me explain in detail how this process happens:

Between 2010 and 2012, the Nigerian Petroleum Development Company (NPDC), the upstream operating arm of NNPC, signed a number of Strategic Alliance Agreements (SAAs) with private Nigerian oil companies. The companies in question were Septa Energy Nigeria Ltd. (Septa), a subsidiary of UK-based Seven Energy (Seven), and Atlantic Energy Drilling Concepts Ltd. (Atlantic), a young Nigerian firm. The SAAs were supposed to support the development of eight onshore oil blocks in which the Shell Petroleum Development Corporation (SPDC) had recently sold its 45% joint venture (JV) minority stakes to indigenous companies. These buyers basically stepped into SPDC's shoes, becoming NPDC's new JV partners on the blocks in question.

Block(s)	Minority Shareholders
OML 4, 38, 41	Seplat
OML 26	FHN and Afren
OML 42	Neconde and KulczykOil
OML 30	Shoreline and Heritage Oil
OML 40	Elcrest and Eland Oil & Gas
OML 34	ND Western and Petrolin

NPDC then elected to serve as operator for most of the blocks, yet it apparently lacked the requisite capital and technical experience to carry out this role alone. So it turned to Seven and Atlantic, assumedly to help bridge the gaps.

There has been much speculation in the press and elsewhere about whether the process for awarding the SAAs was in accord with due process, the requirements of federal procurement law, and the Constitution. The legal opinions I will refer to later discuss these issues exhaustively.

Under each SAA, the Strategic Alliance Contractor agrees to provide technical services and funding to NPDC in exchange for rights to portions of the oil produced from the block(s). More specifically, the agreements call on the Contractor to:

- 1) "Provide all the funds required for NPDC's 55% Petroleum Operating Costs".
- 2) Recoup the capital provided to NPDC in kind, in "cost oil" or "cost gas". This means that part of the 55% of total oil production that would otherwise belong to NPDC is re-allocated to the Contractor, who is free to sell the oil on its own terms and retain profits.
- 3) The Contractor and NPDC split government's equity share of any remaining profits from the blocks. (I have attached as Appendix 12 the SAA between NPDC and AE for OML 30).

The transparency of these arrangements is quite low, while their complexity is high. The SAAs foresee "cost" and "profit" oil from the blocks being split between NPDC

and the partner using a complex accounting mechanism (see e.g., Atlantic SAA for OML 30, Appendices C-E). Even on paper, these provisions can be difficult to follow.

How the oil is divided in practice is unfortunately no clearer. Thus far, NNPC has not published or otherwise disclosed detailed information on flows of money or oil around the blocks covered by SAAs. To the best of my knowledge, neither have any independent audits been conducted.

As with the swaps, if to a somewhat lesser degree, these SAA deals involve substantial amounts of oil production. By July 2013, the eight blocks said to be covered by SAAs appear to have been producing around 130,000 b/d. It is my understanding that both Contractors lifted fairly regularly last year, in amounts as low as 23,000 barrels to over 600,000 barrels at a time. Given that oil from the blocks is exported through the Forcados terminal, Shell, the terminal operator, apparently marketed the crude for them internationally. We do not know exactly how much of NPDC production comes from these blocks.

The document marked Appendix 11 explains the income sharing formula in the SAAs. Please turn to page 3 and note the opening sentence of the first paragraph on that page. It reads:

"NPDC holds a 55% legal interest in and is the operator of OML 26, OML 30, OML 34 and OML 42. As part of the SAA's attributed to these leases, the SAA contractor (Atlantic Energy) pays NPDC's share of OPEX and CAPEX cash calls. Atlantic Energy then receives 100% cost recovery of the OPEX and CAPEX cash calls and a 20-70% share of NPDC's profit oil and gas, from its 55% working interest. The SAA contractor receives its entitlements from independent oil lifting rights".

The illustration at the top of the page shows the situation clearly. There are many questions around these transactions that are not directly necessary to go into at this particular time. Do Seven Energy and Atlantic Energy have any strong track record in crude oil production? One has mainly focused on marginal gas fields, the other in the physical trading of oil and fuel. Are the two companies related? Two co-founders of Seven Energy now hold themselves out as Co-CEO's of Atlantic Energy.

They are also collaborating on a high profile philanthropic vehicle called the made in Africa Foundation. A confidential review by the Banking Supervision Department of CBN suggests that Atlantic Energy is jointly owned by these two persons through their shareholding in the parent company, Atlantic Energy (British Virgin Island) Ltd. This ownership is masked by placing the shares in Geneva Wealth capital management (GWCM), nominees of Switzerland, which holds them in trust for them.

If these companies do not have the experience in crude oil production to have been given this operatorship, why are they chosen as operators? The CV of the CEO of NPDC shows that he is better qualified than either CEO of these companies to run crude oil production business. There is also little evidence that they brought in any capital of their own. Atlantic Energy borrowed money from Nigerian banks secured by its oil lifting under the SAA. In other words they used the 55% of the blocks "owned" by NPDC as the base for raising finance.

I have attached as Appendix 13 a document showing how revenues are lost due to the lack of experience and financial clout of these Operators. So now that we have a full understanding of the SAAs we come to the main point here. What exactly is the role of NPDC in this transaction? It is clearly not the operator, even though there is nothing that is done by Atlantic Energy or SEPLAT that NPDC management cannot do.

The answer is simple: NPDC has been used by NNPC as an SPV for the purpose of acquiring assets belonging to the Federation and transferring the income to private hands.

The Federation was effectively the equity holder in the Joint Venture, and the entire profit crude from its 55% is to be paid into the Federation Account according to the Constitution. Mr. Chairman, NNPC, which was managing this Joint Venture on behalf of the Federation unilaterally took over the Federation's interest and handed it over to its subsidiary not to manage, but to own. This subsidiary therefore has been keeping income due to the Federation for its own use. In addition, the income was further alienated by signing SAA's with parties who had neither the technical expertise nor the capital to develop the joint venture, but who are none-

the-less able to lift crude and retain the proceeds in the name of recovery of opaque costs and up to 70% of the profit of the Joint Venture.

The Federation, having been deprived of its equity crude income, receives nothing but tax from NPDC. For example, in addition to the \$6b worth of crude NNPC lifted for NPDC in this period (Jan' 12 – July' 13), NPDC and Atlantic Energy lifted over \$1b worth of crude in their own name. (Schedule is given in Appendix 14).

In this period, NPDC paid PPT of less than \$400m (see Appendix 15). Atlantic Energy pays no tax and no Royalty. So out of the \$7b crude shipped by NPDC/AE, which ought to come to the Federation Account, only \$400m or so has come in, in the form of tax paid by NPDC. Mr. Chairman, you will note that from Appendix 13, the entry fee paid to Shell for its 45% stake in the blocks was \$2.3b. This means the value of the Federation's joint venture share was in excess of \$2.8b. This was taken from the Federation and handed over to NPDC.

Mr. Chairman, in order to be certain that this transaction was unconstitutional and that the entire income taken by NPDC and its partners belongs to the Federation I requested for, and obtained, three independent legal opinions on the matter. Please find attached opinions from:

1. Konyinsola Ajayi, SAN of Olaniwu Ajayi (Appendix 16)
2. A B Mahmoud SAN of Dikko & Mahmoud (Appendix 17) and
3. Abubakar Ndakene Esq of LAWLEAD Consult (Appendix 18)

All three opinions are clear. The income from these blocks should go to the Federation Account. But this is not all. As is evident from the reviews of the SAA, there are a number of troubling issues. The SAA is treated as a Financing Agreement, and therefore a service contract. This means only NPDC pays Petroleum Profit Tax. Atlantic Energy pays no PPT or Royalty on its Crude. Secondly, customs duties etc. are treated as "Development Cost" and recoverable from "Cost Oil" and "Cost Gas". This means NNPC has effectively given AE tax relief, by refunding any duties paid through Crude that should be Federation income. There are even some indications that this company has exemption from Corporate Profits Taxes.

The net effect of these SAAs, to summarize is as follows:

NNPC transfers its JV interest in the blocks to NPDC. NPDC now transfers that interest to the SAA partner without fair consideration and transfers revenues to them without justification. They bring neither technical competence nor financial clout to the table. The money they have brought in was from loans from Nigerian banks made possible by the same SAA, and some "reinvestment" of money from proceeds of Crude sold.

The Partners take the income, do not pay any taxes to the Federation, and NPDC pays PPT on the residual. NNPC does not transfer the income earned to NPDC as dividend to the Federation Account. So the SAAs simply transfer Federation income to NNPC, NPDC and their business partners.

Until this SAA arrangement is audited and investigated, it is safe to reject the explanation that \$6 b belongs to NPDC.

Oil Theft and Bunkering

Mr. Chairman, I have explained that the interest of the CBN in this matter is driven by our responsibility for protecting the external value of the Naira and managing the Country's external reserves. Both functions are threatened by failure of NNPC to remit the correct amount of Oil revenues to the Federation Account.

We recognize that NNPC is not the only source of revenue loss. For this reason, the CBN commissioned Global Financial Integrity to carry out a survey of oil theft and bunkering in the Niger-Delta. The final report, which I am making available in public for the first time, estimates a revenue loss of \$6.5b - \$12b annually at a price of \$100pbbl. The report was based on interviews with oil thieves, bunkerers, illegal refiners, oil industry practitioners and public officers. The report also involves satellite imagery analysis over a 5 year period and identifies the exact location of bunkering vessel clusters and every illegal refinery located in the Niger-Delta. It is evident that the bulk of oil theft, bunkering and illegal refining have been happening in the more recent periods, mainly 2010-13 when you look at the images. The point here is that the CBN has been looking at all angles of this phenomenon with a view to understanding and finding a solution to these losses.

Summary

We believe the pressure on the reserves of the Federation and exchange rate coming from weak oil revenue in spite of strong oil prices is coming from three principal sources, all of which are entirely within our country's control:

1. Fiscal terms of PSCs and the structure of production. We have already shown that these terms can be re-negotiated without recourse to a PIB;
2. Oil theft and Bunkering in the Niger-Delta. The report we have given you shows that this can be addressed at low economic cost with the right amount of political will;
3. Illegal and unconstitutional acts on the part of NNPC leading to non-remittance of revenues to the Federation Account. We have shown that this takes the following forms;
 - 1) "Up-front" deduction for subsidy for PMS while side-tracking PPPRA, the agency set up for the purpose of verifying and paying subsidies. If NNPC cannot produce documents proving that this subsidy was truly earned, this should be the basis for a major investigation. The entire subsidy claims of NNPC for 2010-2013 need to be audited given divergence from historical norms and increased opacity. NNPC should be compelled to produce proof of each claim to an independent auditor at the minimum.
 - 2) Illegal and unauthorized payment of rent on kerosene which is not a subsidized product and in violation of a written directive from the President. Various committees (Aig-Imoukhuede, Farouk Lawan, Nuhu Ribadu, KPMG etc.) have alerted the nation on this but nothing has changed. Again the burden of proof is on NNPC to show its authority for doing this.
 - 3) The transfer of revenues from oil blocks to NPDC and its business partners like Seven Energy and Atlantic Energy. Also, entering into agreements that effectively gave its business partners tax relief and waivers. (see Appendix 17 for example)

- 4) Crude for Product Swap Contracts that contain loopholes through which revenues keep leaking. We do not have full visibility on the exact losses but have provided sufficient grounds for investigation.

In the period under review, our considered opinion is as follows:

- 1) The \$12 billion shortfall in Domestic crude repatriation needs to be independently investigated considering the clearly unreliable statements coming from NNPC. This is in addition to a full investigation of the entire N2 trillion allegedly claimed in 2011. The burden of proof is on NNPC once it is established that they made the claims. The N180b claim in Q1:2012 needs PPPRA ratification.
- 2) The \$6 billion NNPC claimed it shipped on behalf of NPDC, plus the \$1 billion shipped by NPDC & Atlantic Energy need to be audited. At least a part of that income belongs to the Federation Account as it was produced under SAAs.
- 3) The \$2b claimed as Third-party financing needs to be verified and proven. This means we still have questions over \$20b in the period, even though part of this may be explained with appropriate documentation.

Mr. Chairman, I do not believe this matter will be resolved in a "reconciliation meeting" among CBN, NNPC and Finance. Once it is agreed that NNPC has been spending Federation money, the only solution is an independent investigation in which NNPC is legally compelled to produce documentary proof of its claims. In 2011, Transparency International reviewed 44 National Oil Companies as part of its report on oil and Gas Companies Promoting Revenue Transparency. NNPC was ranked the least transparent; it earned a perfect score of 0% on organizational disclosure. (See Appendix 30).

Every investigation into revenues of NNPC has been met by failure to produce documents. This was the experience of KPMG, Nuhu Ribadu, Aig-Imoukhuede, Farouk Lawan, NEITI, RMAFC etc. NNPC has not published audited accounts for many years.

Finally, over the past few years I have reviewed dozens of documents and reports from within the CBN and other sources. I have not seen a single document showing that NNPC was authorized either by the President or the petroleum Minister to carry out these acts. Our position therefore is that these losses are entirely the responsibility of NNPC and its management and we can put a stop to this.

Recommendations

I would like to make the following recommendations going forward:

- 1) NNPC should stop collecting 440,000bbl daily as "Domestic Crude". The amount of crude should be reduced to the refining capacity of its refineries based on a signed refining contract that clearly states what products are to be delivered for each barrel taken. Sale proceeds net of recognized processing costs are to go to the Federation Account;
- 2) All crude for Product Swaps should be terminated and crude should be exported and sold at market price
- 3) Where NNPC needs to generate cash flow to fund PMS Imports, it can "borrow" crude, on the approval of the Finance Minister, for 90 - 120 days. This crude is to be valued at the ruling market price. NNPC may sell the crude, import PMS and sell through its outlets. It should claim subsidy from PPPRA like every other marketer and present all required documents. Thereafter NNPC should pay back the full value of crude lifted to the Federation Account and retain the profit. Where NNPC delays payment the amount outstanding should attract interest at commercial rates until payment.
- 4) All the SAAs entered into by NPDC should be investigated for constitutionality. The production numbers, Opex and Capex, and profit shares should be audited. The tax arrangements entered into with these parties should be reviewed and all revenues due to the Federation collected. If possible the SAAs should be terminated. Certainly, NNPC should be prohibited from entering into any SAAs in the future.

- 5) NNPC to account for subsidies claimed in 2010-13 by producing documentary proof of legitimacy. Also to produce their authorization for paying kerosene subsidy after July 2009.

As for what action needs to be taken on what has happened in the past, we express no opinion. The decision on what to do in this case rests entirely with the Government. My task is limited to raising an alarm over what I think is a development that is harmful to the economy, and establishing that the alarm was neither spurious nor baseless. I still insist that an investigation is needed to establish the extent of the losses and the nature of offence committed.

I believe I have placed enough information before this committee to make the point. The amount in 19 months may be \$10.8 billion or \$12 billion or \$19 billion or \$21 billion, we do not know at this point but if we extend the period the amount will increase anyway, since this has been going on for a long time. The first priority is to stop it. It is unsustainable, and it will ultimately, if not stopped, bring the entire economy to its knees.

Please remain assured of my highest regards.

Sanusi Lamido Sanusi (CON)
Governor, Central Bank of Nigeria