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Country Experience with EITI – Part 1

Twenty-seven countries are at various stages of implementing the Extractive Industries Transparency Initiative (EITI). One of the earliest implementers, Nigeria, estimates that EITI helped increase petroleum revenues to the government by US$ 1 billion in 2004 and 2005. This note reviews the EITI implementation and related experience of some countries, focusing primarily on actions taken by governments in oil-producing countries.

“We are looking at close to a billion dollars saved,” the Executive Director of Nigeria EITI (NEITI) told news reporters in January 2007, attributing the additional revenues to the close monitoring of the oil companies in 2004 and 2005 under NEITI [1]. EITI, through multi-stakeholder partnerships, supports improved governance in resource-rich countries through the verification and full publication of company payments and government revenues from oil, gas, and mining [2, 3].

If the criterion for being resource-rich is that at least 25 percent of the government’s total revenue or of total export proceeds is from oil, gas, or mining, then 50 countries were resource-rich based on the data from 2000–2005. The region with the largest number of resource-rich countries was Africa (18), followed by the Middle East (11), the Americas (8), Central Asia (6), East Asia (5), and Europe (2). The resource-rich East Asian countries were Brunei, Indonesia, Vietnam, Mongolia, and Papua New Guinea, of which the last two are mineral-rich. Other Asian countries, such as Timor-Leste and Cambodia, are already resource-rich or have the potential to become so in the future. To date, 27 countries have publicly committed to EITI, including Mongolia and Timor Leste in East Asia. Eight countries have issued one EITI report or more. No two EITI programs are alike; each country has adapted and added to the EITI criteria to suit its particular circumstances and objectives.

In terms of scope, the country with the widest coverage is arguably Nigeria, perhaps reflecting the desire and determination to redress decades of oil revenue mismanagement (see [4]). NEITI takes EITI as a starting point and tackles a host of other issues that EITI criteria do not cover (see “EITI in Context” in [3] for what the criteria do not cover). São Tomé and Príncipe and Timor-Leste have legislated revenue disclosure. This briefing note covers Nigeria in some detail on account of its comprehensive coverage, extensive outreach to civil society, and the lessons it offers for the management and accountability of the petroleum sector. It is the first of a two-part series describing the experience of these and other countries.

Nigeria

Nigeria has a long history of oil production and is Africa’s largest oil producer. Oil revenue accounts for more than 40 percent of the country’s gross domestic product (GDP), 80 percent of government revenue, and 90 percent of total exports. President Obasanjo committed the government of Nigeria to EITI in November 2003 and launched NEITI in February 2004.

The NEITI process consists of financial, physical, and process audits. Physical and process audits are not required by the EITI criteria [3], but NEITI has included them to strengthen governance in the sector. The first complete set of reports, covering the six-year period from 1999 to 2004, was published in April 2006, about 2½ years after Nigeria first endorsed EITI. The report represented the most comprehensive audit of the petroleum sector in Nigeria’s history. The administrator (for reconciling payments and revenues; see [3]) for the audit covering 2005 is being contracted. The tender for the 2006 audit, which will include the so-called value-for-money audit of petroleum sector processes—examining whether expenditures are reasonable and prudent—will be issued in the second half of 2007.

The financial audit is at the heart of EITI. The principal benefit streams examined in the 1999–2004 audit were:

- Oil related flows: petroleum profit tax, royalty, gas flaring penalty, reserves additional bonus, and signature bonus
- Non-oil related flows from the petroleum sector: value-added tax, education tax, and withholding and PAYE (pay as you earn) tax to federal and state governments
- Proceeds of sale of crude oil and gas allocated to the government (typically the largest of all inflows to the government), and cash-call payments made by the government (representing financial outflows), in accordance with the government's equity share in joint venture operations.

The audit covered material payments from 22 companies as well as government financial flows through seven joint venture operations. The findings were reported by company and payment type. This audit also published a report entitled "Issues in Government Financial Systems," which outlined the difficulties encountered during the financial audit and made recommendations to improve government accounting for better management and control of key revenue sources in the petroleum sector. Subsequent work by the administrator identified weak recording practices in the government agencies as the primary cause of the discrepancies, and reduced the unexplained discrepancies to 0.01 percent [5]. The final audit report was released to the public in December 2006. Inter-agency reconciliation processes have been simplified and improved as a result of using the reporting templates.

The physical audit carried out a material balance on hydrocarbons (oil and gas) in the country—that is, tracing the volume of hydrocarbons from production to the final point of sale. The audit covered hydrocarbons produced, lifted, flared (for gas), lost, refined, and exported; refined products imported; and all refined products supplied on the domestic market. Significant inconsistencies in volumes were found as well as shortcomings in metering and book-keeping. The audit found a systematic loss of crude oil between the wellhead and terminals. Fluctuations in the pipeline flow rates suggested thefts at night [5]. The audit report made several recommendations to strengthen physical accounting.

The process audit reviewed the transparency and efficiency of refinery operations and refined product importation; capital and operating expenditures; oil and gas licensing processes; the process for marketing natural gas; and the process for marketing the federal government's equity crude oil. A large number of recommendations were made in a series of reports issued under process audits. Thanks to public-awareness raising and publicity in the media, issues such as transparency of the oil licensing rounds have been widely discussed.

In response to these findings and recommendations, President Obasanjo in May 2006 directed NEITI to set up and chair an Inter-Ministerial Task Team to address the problems identified in the audit, including institutional weaknesses, poor record-keeping practices, inadequate accounting systems, and poor interface among government entities. The Task Team was constituted and began meeting in August 2006. The relevant government agencies proposed their own remediation measures, set up study teams, and established an inter-agency committee to ensure consistency of information across the government. Steps are being taken to provide assistance to government agencies to strengthen capacity for interfacing with each other. NETI is now being extended to cover the mining sector [5]. Additional information on NEITI activities is available on the NEITI website [6].

The champion of EITI is the Director General of the Nigeria Geological Survey Agency. A 28-member National Stakeholders Working Group (NSWG), established in February 2004 by President Obasanjo, steers implementation. NSWG draws members from civil society (2 representatives), media (1), government (14), local and multinational companies (3), the private sector (4), the National Assembly (2), and the Houses of Assembly at the regional government level (2). The NEITI Secretariat coordinates the work of NSWG, which has technical, legislative, focal (for capacity building), civil society, and media teams. The civil society team engages the wider public and helps build capacity within civil society organizations (CSOs). Capacity building is aimed at helping CSOs understand how EITI works so that they can ask the right questions; educate their constituency and the general public about the oil industry and its revenues; and gain a better understanding of the data and information contained in EITI reports so that they can disseminate information more effectively. NSWG recognizes the limitations of traditional media (newspapers, television, radio) for rural populations and communication difficulties in a country with more than 500 languages, and places emphasis on dissemination of information through a grassroots-based communication strategy and the engagement of rural communities and regional CSOs. NEITI has conducted several "road shows" around the country to interact with civil society representatives and disseminate information, including audit findings. Training of government leaders, legislature, and civil society on petroleum economics, the flow of funds, and the role of NEITI is underway.

In February 2006, a memorandum of understanding (MoU) was signed between NSWG and CSOs with a view to advancing civil society's participation in NEITI, ensuring independence of CSOs in the NEITI process, helping to build CSO capacity, and ensuring proper internal communication among CSOs. Civil society involvement in EITI in Nigeria has helped government ensure that the EITI process leads to enhanced revenue collection, encourages all companies to provide revenue data, helps identify possible sources of oil theft, and contributes greatly to strengthening the quality of public debate about oil issues nationally.

In June 2007, the government passed an NEITI Bill into law. This legislation guarantees mandatory annual audits of the extractive industries sector; oil companies will be legally required to disclose payments; and the recently established Oil Revenue Monitoring unit will be made formally independent of the Finance Ministry and merge with the NEITI Secretariat.

Legislative Approach to Disclosure

São Tomé and Príncipe endorsed EITI principles in June 2004. The country is not yet an oil producer, but has already taken significant steps to write transparency provisions into legislation. An Oil Revenue Law was unanimously approved by the National Assembly and signed by the president in December 2004. This law requires all oil payments to be deposited directly into a national oil fund held by an international custodial bank. Deposits, withdrawals, and holdings of the fund are made public through a newly established public information office and by posting on the internet. The law requires competitive tenders for oil contracts, makes all oil contracts public, mandates the inclusion of anti-corruption and transparency provisions in contracts, and declares null and void those confidentiality clauses in oil contracts that are at variance with the transparency requirements of the law. There is therefore a firm legal basis for São Tomé and Príncipe to implement EITI once commercial production starts.

Timor-Leste is a new natural gas producer. Like São Tomé, Timor-Leste has also taken significant steps to ensure transparency in its petroleum sector, and involved civil society in the process. In October 2004, the government released a "Public Consultation Discussion Paper on Establishing a Petroleum Fund for Timor-Leste." A series of public consultation sessions were held in every district of the country and written comments were submitted. The government released a draft Petroleum Fund Law in January 2005 and further public consultation followed, including testimonies given by CSOs before the Parliament. The Law was passed unanimously in June 2005.

The law requires all revenues associated with petroleum operations to be deposited into the newly created Petroleum Fund. The law cites transparency as a fundamental principle. It stipulates that quarterly reports on the performance and activities of the Petroleum Fund must be published, and that an internationally recognized accounting firm be appointed as an independent auditor of the Petroleum Fund. The auditor's annual report, which states the aggregate amount of payments made by each payer, must also be published. A consultative council that includes members of civil society and the business community is tasked with advising the Parliament on matters related to the Fund's performance and operation, and effective use of appropriations from the Fund. According to the law, monies from the Fund spent by the government (in accordance with the "estimated sustainable income") must flow through the state budget.

The government of Timor-Leste has set up a Petroleum Transparency website in English, Portuguese, and Tetum (a local language) [7]. Posted on the website are the quarterly reports on the Petroleum Fund, various laws related to the petroleum sector (Petroleum Act, Petroleum Taxation Act, Petroleum Fund Act), model production sharing contracts, and sample contracts and their amendments, as well as an earlier version of the Petroleum Fund Act and various comments submitted on the Petroleum Fund discussion paper. Such commitment to disclosure by the government helps build a general climate of accountability and transparency in the sector. The first meeting of the national EITI working group was recently convened in Dili.

Other Countries

Mongolia

Mongolia is the second of the two East Asian countries implementing EITI. A significant producer of copper and gold, Mongolia committed to EITI in December 2005. It has made rapid progress in the last 18 months and has established a multi-stakeholder working group as well as a work plan. Mongolia is currently in the process of setting up a secretariat, whose first task is to appoint an administrator.

Kazakhstan

Kazakhstan, the largest oil producer in Central Asia, committed to EITI in June 2005. Kazakhstan is where Mongolia is in the EITI process, having created a multi-stakeholder working group and a work plan, and being in the process of establishing a secretariat.

Gabon

Oil accounts for about one half of GDP, two-thirds of government revenue, and 80 percent of total exports in Gabon. Gabon committed to EITI in March 2005 after issuing a ministerial decree to establish an EITI Working Group a month earlier. The Working Group includes representatives of all administrations involved in oil revenue collection and management. A stakeholders' group responsible for EITI implementation is chaired by a representative of the President's office and includes representatives from the prime minister's office, ministerial departments, civil society, the oil sector, and the mining sector. A website was launched in October 2005 and the government published, in December 2005, an EITI report covering 2004. The stakeholders observed that the first EIEI report omitted a major revenue stream, which was subsequently included in the second report. However, not all oil companies have reported, and the administrator has not made attempts to reconcile the discrepancies between payments and revenues.

Observations

Nigeria's first EITI report was ambitious and covered six years and a range of issues beyond payments and revenues. By publicly highlighting the weaknesses that needed attention, NEITI has already achieved the objective of quantifying where the gaps are, identifying the likely causes, and recommending remedial actions. Nigeria's experience also suggests that, by providing greater scrutiny over revenue collection, EITI can lead to increased (or more efficient) revenue collection.

Gabon's experience shows that one barrier to providing an adequate level of detail in reporting is poor availability of data on financial flows. It also shows that, absent a legal obligation to report, participation of all companies, without which meaningful comparison of payments and revenues cannot be made, may be difficult.

References

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