

How Shell, Total and Eni benefit from tax breaks in Nigeria's gas industry

The case of Nigeria Liquefied Natural Gas Company (NLNG)

**SOMO**

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Mark van Dorp

Amsterdam, January 2016

Colophon

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The Centre for Research on Multinational Corporations (SOMO) is an independent, not-for-profit research and network organisation working on social, ecological and economic issues related to sustainable development. Since 1973, the organisation investigates multinational corporations and the consequences of their activities for people and the environment around the world.



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Executive summary

This report presents a case study of Nigeria Liquefied Natural Gas Company (NLNG), Nigeria's largest gas production facility, and examines the way in which its foreign shareholders – Shell (UK/Netherlands), Total (France) and Eni (Italy) – benefit from excessively generous tax breaks provided by the Nigerian government. The report sets out the implications of these tax breaks, including the potentially lost tax that could otherwise be used to support Nigeria's public services.

Nigeria Liquefied Natural Gas Company (NLNG), the joint venture in which these companies have a majority stake (51%), has been awarded a 10-year tax holiday thanks to the NLNG Act – an act of parliament created specifically for the venture (in all other cases, new companies investing in Nigeria are given a tax exemption period of three to five years maximum). This special law has resulted in NLNG paying zero taxes for a total period of 12 years: ten years because of the tax break and two further years because of unused tax benefits built up during the 10 years of the tax break. In this report, SOMO has calculated that the total potential lost tax to the Nigerian government amounts to a staggering US\$ 3.3 billion. Due to a number of conservative assumptions, this should be considered a minimum estimate.

SOMO aims to contribute to the discussion on responsible tax governance and financial transparency through this report by presenting factual evidence that tax breaks given to multinational corporations create unacceptable advantages for them that work against the interests of the Nigerian public. The ultimate goal is to raise public awareness of the use and (negative) impacts of tax holidays by multinational companies, using Nigeria as an illustration. It also serves to inform the policies of the Nigerian Government and recommends reconsidering the use of tax breaks to stimulate foreign investment, and to ensure that foreign companies paying their fair share of taxes in Nigeria.

Context of the research

There are different ways to reduce the tax contribution of multinational companies, including tax evasion and tax avoidance; the former is illegal while the latter is legal if morally questionable. There is another way in which companies can reduce their tax contribution – tax incentives provided by governments. A tax incentive (also known as a tax break) is in essence a tax deal given to a company (or to a sector as a whole) to encourage it to invest. But tax breaks as instruments to promote foreign direct investment are increasingly discouraged, as their effectiveness is disputed by the International Monetary Fund (IMF), the Organisation for Economic Cooperation and Development (OECD) and others, and the losses to developing countries are enormous.

Nigeria Liquefied Natural Gas: a key player in the Nigerian economy

Nigeria Liquefied Natural Gas Company (NLNG) – Nigeria's major liquefied natural gas company – is a joint venture between the Nigerian government and three foreign companies: Shell, Total and Eni. The company started commercial operations in 1999 to harness Nigeria's vast natural gas resources and produce liquefied natural gas (LNG) and natural gas liquids (NGLs) for export. It extracts natural gas from the ground, purifies and liquefies it to make LNG, and pipes it to customers.

The NLNG gas production facility is located on Bonny Island, on the southern edge of the Niger Delta – the center of the Nigerian oil and gas industry. The company is jointly owned by Nigerian

Box 1: What is Liquefied Natural Gas?

Liquefied natural gas (LNG) is gas that has been cooled to about -162°C (-260°F) for shipment and/or storage as a liquid. The liquid volume is about 600 times smaller than it is in gaseous form. In this compact form, natural gas can be shipped in special tankers to terminals in other countries. At these terminals, the LNG is returned to its gaseous form and transported by pipeline to distribution companies, industrial consumers and power plants. Liquefying natural gas provides a means of moving it long distances where pipeline transport is not feasible, meaning that regions with vast reserves, but which are too distant from end-use markets to be connected by pipeline, such as in Nigeria, can gain access to those markets more easily.¹

¹ US Energy Information Administration website, "What is LNG?", 2014, <http://www.eia.gov/energyexplained/index.cfm?page=natural_gas_lng> (1 April 2015)

National Petroleum Corporation (49%), Shell Gas B.V. (25.6%), Total LNG Nigeria Ltd (15%) and Eni International N.A. (10.4%). The main destination for the gas is Europe, which accounts for 80-90% of the facility's total production. NLNG made a total profit of around US\$ 29.5 billion over the period 2004 to 2013. As the 49% shareholder, the Nigerian state oil company NNPC has received a large part of these profits.

The cost of extending NLNG's tax holiday to 10 years

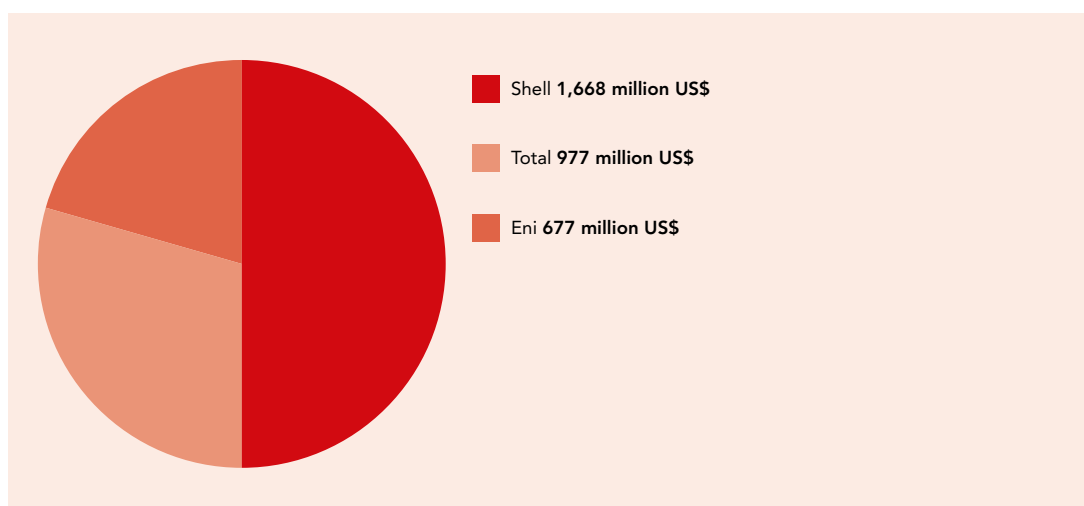
Based on publicly available NLNG financial reports (obtained from the Nigerian company registry), SOMO has compared the potentially foregone Nigerian government tax revenues that result from the NLNG's extended 10-year tax holiday (as established by the NLNG Act) with what would have been received if it had been granted the usual five-year tax holiday which all other companies in Nigeria qualify for under the Industrial Development (Income Tax Relief) Act 1971.

Factoring in a further two years of applying other legal provisions (for example, the carrying forward of deferred tax assets) means the company actually enjoyed a 12-year tax holiday between 1999 and 2011, reducing its tax bill to almost zero during these 12 years. Based on a calculation of the potential amount of tax that would have been payable by NLNG in case of the normal tax relief period in Nigeria of five years, the total potential in lost tax to the Nigerian government amounts to a staggering US\$ 3.3 billion between 2005-2013 – an average tax loss of around US\$ 367 million per year.¹ In a country where more than half of the population lives below the poverty line, Nigeria's citizens could have benefited enormously from these foregone tax payments.

¹ This is the total potential tax lost to the Nigerian government for all three companies together, comprised of non-paid corporate income tax and education tax. Due to a number of conservative assumptions, this should be considered a minimum estimate.

The estimate of US\$ 3.3bn cost to the Nigerian government is a conservative estimate. First, the calculations only include lost tax revenues from the three private companies' share of the joint venture; 51% of the total. Second, it only calculates lost tax revenues from two taxes: corporate income tax and education tax. It excludes all other taxes exempted under included in the tax holiday. Third, at the end of 2013 US\$1.15bn was still owed to the Nigerian government as tax obligations from 2012

Figure 1: Share of potentially lost tax to the Nigerian government directly attributable to the three companies over the period 2005 - 2013



These calculations take account of the fact that the Nigerian government has a 49% stake in NLNG, which means that part of the tax lost theoretically flows back into the Treasury, although it is unclear through which channels. In other words, the calculations in this report are limited to the private companies' stake in the business, or 51% of the foregone tax, which was lost to the Nigerian government. As shown in Figure 1, tax potentially lost to the Nigerian government which is directly attributable to the three companies can be broken down as follows:

- ▣ For Shell, based on its 25.6% interest in NLNG, this amounts to around US\$ 1.7 billion.
- ▣ For Total, based on its 15% interest in NLNG, this amounts to US\$ 977 million.
- ▣ For ENI, based on its 10.4% interest in NLNG, this amounts to US\$ 677 million.

New tax law will allow even more companies to obtain 10-year tax breaks

Apart from Nigeria LNG, to date no other companies in Nigeria have benefited from a 10-year tax holiday enacted by law. However, recently a bill to amend the Companies Income Tax Act 2004 was passed at the Nigerian National Assembly. The proposed amendment aims to provide additional tax incentives for the gas and mining sectors, and businesses located in areas with inadequate infrastructure, and includes an extension of the period for tax holidays to 10 years for all companies operating in Nigeria. This bill is expected to lead to even fewer foreign companies paying their fair share of taxes in Nigeria – a country that already has a problem in ensuring sufficient domestic revenue

mobilisation from the private sector and from ordinary citizens alike. As a consequence of this new bill, Nigeria's only substantial source of taxation (companies extracting the country's natural resources) will be seriously eroded and foreign companies will be allowed to benefit from tax breaks as massively as the three oil companies in this case study did.

Key conclusions and recommendations

- ❑ Royal Dutch Shell, Total and Eni, as majority owners of the joint venture Nigeria LNG (51%), are exploiting natural liquefied gas in Nigeria at a bargain price due to an extended 10-year tax holiday – a tax break double what any other company was given when starting a business in Nigeria. In addition, due to other legal provisions including the carrying forward of deferred tax assets, the company's tax bill was reduced to almost zero during the first 12 years of operation, instead of the standard period of 5 years.
- ❑ SOMO's calculations show that this tax holiday has been extremely costly for Nigeria, but very beneficial for the three private sector partners in the NLNG venture. The tax incentive, which became law through an act of parliament, appears in principle to have been subject to democratic scrutiny though there is no information regarding whether the three companies Shell, Total, and Eni influenced the enactment of the NLNG Act. It is however doubted whether the NLNG Act has been beneficial for Nigeria, given the high amounts of tax potentially lost to the Nigerian government.
- ❑ This case study provides a clear illustration of the negative economic impacts of tax breaks given to foreign companies in oil- and gas producing developing countries. The Nigerian government's use of very generous tax breaks – and the willingness of multinational companies to use these tax breaks – needs to be questioned as it has been shown to have harmful impacts on governments and citizens in the host countries.
- ❑ There is no account publicly available on how the Nigerian government (a 49%-shareholder in NLNG) has spent its share of the dividends. NLNG's total profits amounted to at least US\$ 29.5 billion over the period 2004 to 2013. In Nigerian Extractive Industries Transparency Initiative (NEITI) audits, questions have been raised about who actually benefits from NLNG's operations: the Nigerian federation, the federal government, or the Nigerian state oil corporation (NNPC) itself?
- ❑ The Nigerian government is demanded to provide more clarity on how this extended tax holiday and the NLNG Act came into being, and on the reasoning behind the granting of a 10-year tax holiday instead of the standard five-year period in Nigeria.
- ❑ The Nigerian government is demanded to:
 - publish any costs-benefit analysis or arguments behind the NLNG Act and publicly explain the reason behind the ten-year tax holiday to the Nigerian people;
 - make a cost-benefit analysis of current tax incentives granted to the Consortium and propose to change the Act as appropriate.

- ❑ The Nigerian Parliament is demanded to:
 - revoke the proposed amendment to the Companies Income Tax Act, which aims to extend pioneer status tax holidays from 5 to 10 years;
 - investigate the process that led to the NLNG Act, and make the findings known to the Nigerian public;
 - demand that the executive arm of government follows up on the previous government's statement of intent to review the tax incentive practices in Nigeria.

- ❑ Given their corporate responsibility to provide revenue transparency, it is demanded from Shell, Total and Eni to publicly disclose information on sales, the number of employees, profits made and taxes paid in Nigeria, in line with the country by country reporting template² proposed as part of the base erosion and profit shifting (BEPS) process.³ It is demanded that companies publish their accounts from all subsidiaries in Nigeria on their website and make public what they gain from the various tax incentives enjoyed in Nigeria every year. Only by publishing these data will governments, parliaments and citizens know how much the Nigerian public is positively or negatively affected by the three companies in Nigeria. It is also demanded from the three companies that they pay taxes at prevailing rates without seeking tax incentives in developing countries as a requirement to establishing businesses there, and seek a level tax playing field with other corporate taxpayers, domestic and multinational, in all jurisdictions where they operate.

- ❑ As host states of the three multinational companies, it is demanded that the governments of Italy, the Netherlands, France and the UK require that companies registered under specific country legislation report and publicly disclose information on sales, the number of employees, profits made and taxes paid in each country and jurisdiction in which they operate. In promoting international trade/business/investments, resident governments must not engage in political or other activities that will lead to the private sector organisations being offered excessive and harmful tax incentives in other countries.

- ❑ This case study has focused on the overgenerous tax breaks awarded to Nigeria LNG. In addition, it would be interesting to investigate a number of other aspects that raise questions about this company, especially the fact that one of NLNG's wholly-owned subsidiaries, Bonny Gas Transport Ltd, is based in Bermuda, a notorious tax haven. It was beyond the scope of this report to look into this case, but it is recommended to do follow-up research on the Bermuda connection of NLNG.

2 Country by country reporting obliges companies to publish key financial data for each country in which they operate.

3 Base Erosion and Profit Shifting project of the OECD.

List of abbreviations

bb/day	barrels of oil per day
bcm	billion cubic metres
BEPS	Base Erosion and Profit Shifting project of the OECD
BGT	Bonny Gas Transport Ltd
boe/day	barrels of oil equivalent per day
CFO	chief financial officer
CIT	corporate income tax
DTT	non-double taxation treaty
EITI	Extractive Industries Transparency Initiative
EPZ	export processing zone
FDI	foreign direct investment
FIRS	Federal Inland Revenue Service
IOCs	international oil companies
JV	joint venture
LNG	liquefied natural gas
MNC	multinational corporation
mtpa	million tons per annum
NDDC	Niger Delta Development Commission
NEITI	Nigerian Extractive Industries Transparency Initiative
NNPC	Nigerian National Petroleum Company
NLNG	Nigeria LNG Ltd.
OPEC	Organization of Petroleum Exporting Countries
OPL	oil producing licence
PSC	production sharing contract
PWYP	Publish What You Pay
PPT	petroleum profit tax
SCF	standard cubic feet
SEC	Securities Exchange Commission
SEPA	Shell Exploration and Production Africa Ltd
SEZ	special economic zone
SNEPCo	Shell Nigerian Exploration and Production Company Ltd
SOMO	Stichting Onderzoek Multinationale Ondernemingen
SPDC	Shell Petroleum Development Company of Nigeria Ltd.
VAT	value added tax
WHT	withholding tax

1 Introduction

“African nations need to reexamine their own tax systems, and remove currently instated tax exemptions and inherent inefficiencies in those tax systems, in order to raise revenues and fund development.”⁴

Conclusion at IMF conference in Kenya, March 2011

“The pioneer status enjoyed by NLNG was the government’s initiative to encourage the liquefied gas industry at inception. The reasoning then was that government thought Nigeria had more potential in gas than crude, so the thought then was that they needed to develop it, and in doing so, they were given a tax holiday of 10 years, which is abnormal.”⁵

Mr Bamidele Ajayi, Director Oil and Gas of Federal Inland Revenue Service, 2012

This report presents a case study of Nigeria Liquefied Natural Gas Company (NLNG), Nigeria’s largest gas production facility, and examines the way in which its foreign shareholders – Shell (UK/Netherlands), Total (France) and Eni (Italy) – benefit from excessively generous tax breaks provided by the Nigerian government. The report sets out the implications of these tax breaks, including the potentially lost tax that could otherwise be used to support Nigeria’s public services.

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SOMO aims to contribute to the discussion on responsible tax governance and financial transparency through this report by presenting factual evidence that tax breaks given to multinational corporations create unacceptable advantages for them that work against the interests of the Nigerian public. The ultimate goal is to raise public awareness of the use and (negative) impacts of tax holidays by multinational companies, using Nigeria as an illustration. It also serves to inform the policies of the Nigerian Government and recommends reconsidering the use of tax breaks to stimulate foreign investment, and to ensure that foreign companies paying their fair share of taxes in Nigeria.

4 Taxation Info News, “Remove tax exemptions in Africa, says IMF,” 22 March 2011, <<http://www.taxationinfonews.com/2011/03/remove-tax-exemptions-in-africa-says-imf/#ixzz2CBv9aH49>> (15 July 2015).

5 FIRS, “NLNG has enjoyed 10 years abnormal tax holiday” – D/Oil & Gas; 2012, <<http://www.firs.gov.ng/Resource-Centre/Documents/Newsletter%20July%202012%20Vol.%202.pdf>> (1 April 2015).

1.1 Focus and structure of the report

This research paper highlights the case of an excessively generous tax holiday awarded to NLNG, a joint venture in Nigeria between oil giants Shell, Total and Eni, and the Nigerian national oil company, NNPC. Shell has the biggest stake in the joint venture and is the operating company. The ultimate goal is to raise public awareness of the use and (negative) impacts of tax holidays by multinational companies, using Nigeria as an illustration. It also serves to inform the policies of the Nigerian Government and recommends to reconsider the use of tax breaks to stimulate foreign investment and to ensure that foreign companies paying their fair share of taxes in Nigeria.

The report is structured as follows. Chapter 1 sets out the report methodology, as well as the context of the debate on tax incentives. Chapter 2 introduces the three multinational companies involved, Royal Dutch Shell, Total and Eni, with special attention to their policies and practices on tax and transparency. Chapter 3 provides an overview of the oil industry in Nigeria and its tax system. Chapter 4 presents the case of NLNG, focusing on the extended tax holiday awarded to it, and shows how the three oil companies have made huge profits during the first 12 years of operation while reducing their tax bill to almost zero. An estimate is given of the lost tax to the Nigerian government. Chapter 5 presents conclusions and recommendations. In Annex 1, information can be found about the shareholders of NLNG, while Annex 2 provides detailed explanations for the NLNG case study. Annex 3 includes a glossary of technical terms used in this report. Finally, Annex 4 includes the company responses to the draft report.

1.2 Methodology

This report is the result of an extensive research process that started with an assessment of potential cases of tax avoidance by multinational corporations in Africa. After assessing potential “red flags” of tax avoidance for a number of companies in 7 African countries, it was decided to focus on the Nigerian oil and gas industry, given the large economic importance of this sector and the large number of red flags that were obtained for a number of company cases. As a next step, field research in Nigeria was carried out to collect annual accounts for various local subsidiaries of multinational corporations, and to interview local stakeholders on the issue of tax avoidance and tax incentives. After this field mission, that was carried out in close collaboration with ActionAid Nigeria, the decision was made to focus on the case of Nigeria LNG, as it provided the most telling “red flag”, both in terms of economic impact (due to the size of the tax holiday) and in terms of possibilities of outreach to companies, governments and the general public.

The case study was carried out by SOMO, with the support of a number of experts on tax issues, both in the Netherlands and in Nigeria. The report was written in close collaboration with ActionAid, who has published a briefing paper based this report. The first draft of the report was shared with these experts and their comments and suggestions fed into the research process. SOMO has reviewed the findings with the companies involved. The final outcomes remain the sole responsibility of SOMO.

During the research process, SOMO used a number of research tools, including the SOMO Research Manual and its in-house manual on Corporate Case Study Research, which was developed jointly by

SOMO and ActionAid in 2011. Another important source was the civil society tax toolkit, co-produced by SOMO in 2011.⁶

The research process for the case study of NLNG included the following steps.

1. Document search
 - Annual reports and other documents published on the websites of NLNG, Shell, Total and Eni.
 - Documents obtained from search engines, databases and corporate information websites.
2. Desk research
 - Analysis of Annual reports and other company documents for key company data (turnover, taxes paid, profit after tax).
 - Extracting of the company structure for NLNG in Nigeria, including ownership relationships with Shell, Total and Eni, as well as the Nigerian national oil corporation, by using annual reports and company websites.
3. Field research in Nigeria
 - One-week field visit to Nigeria for extended search in the national company registry and interviews with key stakeholders (policymakers, NGOs, tax authorities). This included obtaining the annual accounts for NLNG for the past seven years (2007 to 2013) at the official company registrar in Nigeria (Corporate Affairs Commission in Abuja⁷).
4. Data analysis
 - Analysis of NLNG company accounts, focusing on the use of tax breaks in Nigeria.
 - In-depth analysis of the tax break awarded to NLNG and the relevant tax legislation in Nigeria.
 - Calculation of the amount of potentially lost tax through these practices.
5. External fiscal check
 - The report was reviewed by independent experts for accuracy in the fiscal elements of the report, both in Europe and in Nigeria.
6. Company review
 - Before publication, SOMO and ActionAid have reviewed the findings with the four Shareholders of the joint venture, NNPC, Shell, Total and Eni, as well as with the NLNG management. The questions sent to the companies have been included in Annex 4. This is followed by a description of the way in which the three foreign shareholders as well as NLNG management have responded to the initial findings. No response was received from the Nigerian National Petroleum Corporation (NNPC).

6 Christian Aid and SOMO, "Tax Justice Advocacy: A Toolkit for Civil Society," 2011, <<http://taxjusticetoolkit.org/>> (22 July 2015).

7 See <<http://new.cac.gov.ng/home/>>. It should be noted that annual accounts of companies registered in Nigeria can only be obtained in person in Abuja, as there is no online company registry.

The following methodological remarks can be made:

- ❑ SOMO's findings are based on general, publicly available information on the Nigerian tax system. To ensure that the information used is correct, the aspects related to Nigerian tax law have been checked by a Nigerian tax accountant.
- ❑ The calculations in this report are based on NLNG financial reports obtained from the Nigerian company registry for the period 2007 to 2013. A number of pages were missing in some of these reports, but this has not influenced the calculations as the key data were available.
- ❑ The financial reports for the years 1999 to 2006 have not been consulted, but this has not significantly impacted the results of our calculations since most of the key data for these years were found in annual accounts from later years.

1.3 Background

Fair share of tax

When multinational companies do not pay their fair share of tax, the result is reduced tax revenues for governments in both developed and developing countries – revenues that could be used to combat poverty and stimulate development. This affects national and international development efforts. It also affects both the capacity of developing country governments to provide essential services to their populations and the capacity of developed country governments to provide finance for development in the form of debt relief and official development assistance (ODA), and improve policy coherence for development. Secrecy jurisdictions, more commonly known as tax havens, have been a barrier to increasing taxation of the population's richest sectors and of multinational corporations that operate in developing countries. Several international initiatives have been launched to tackle this situation, including the OECD Action Plan for Base Erosion and Profit Shifting.⁸ Also, improved domestic revenue mobilisation has been included as a key element of the Sustainable Development Goals (SDGs).⁹

Tax incentives

There are different ways of reducing the tax contribution of multinational companies, including tax evasion and tax avoidance. While tax evasion is illegal, tax avoidance is defined as legal but is morally questionable. Tax incentives granted by host governments are another way in which companies can reduce their tax contribution. A tax incentive (also known as a tax break) is, in essence, a tax deal given to a company (or to a sector as a whole) to encourage it to invest. A tax deal is neither tax evasion nor tax avoidance, since it is generally considered within the spirit and the letter of the law.

Tax incentives can be grouped into a number of categories: tax holidays, investment allowances and tax credits, timing differences, reduced tax rates and free economic zones (where tax exemptions are

8 OECD, "Action Plan on Base Erosion and Profit Shifting," 2013, <<http://www.oecd.org/ctp/BEPSActionPlan.pdf>> (15 July 2015).

9 SDG 17.1 focuses on "strengthening of domestic resource mobilization, including through international support to developing countries to improve domestic capacity for tax and other revenue collection", <<https://sustainabledevelopment.un.org/focussdgs.html>> (15 July 2015).

provided to all companies established there).¹⁰ According to an ActionAid report on tax breaks, the estimated revenue foregone through corporate income tax exemptions, based on a 16-country average (consisting of developing countries) was 24% as a share of corporate income tax (CIT) raised, or 0.60% as a share of gross domestic product (GDP). The result is that over US\$ 138 billion is lost by developing country governments every year in statutory corporate income tax exemptions alone.¹¹

Call for abandoning tax incentives

These negative impacts on tax revenues have led NGOs to actively call for abandoning excessive tax incentives and tax holidays. For example, a recent review by ActionAid of recommendations for responsible tax practice by multinational companies indicated that tax incentives are one of the eight key areas of tax responsibility. It concluded that the impact of tax incentives on public revenues is likely to be at least as great as (if not greater than) the impact of tax planning practices, and therefore is an important area for reconsideration.¹² Under tax holidays, new firms are allowed a period of time when they are exempt from paying income tax. Sometimes, this grace period is extended to a subsequent period of taxation at a reduced rate. Tax holidays are often used to attract footloose investment, not limited to, for example, the presence of natural resources. However, it is often the case that investors move on once preferential terms end, rather than making the kind of long-term commitment that brings new skills, technology and links to the local economy. In practice, these tax incentives distort investment decisions – encouraging short-termism – and can lead to ‘churning’, where businesses continually close down only to reinvent themselves under a different name or corporate entity to benefit from a new tax holiday.

Cost of tax incentives to developing countries

And not only civil society cautions against the use of excessive tax incentives. Spearheaded by the IMF, the tendency internationally has been to advise governments to abandon tax incentives, as their effectiveness is disputed and the losses they cause for developing countries are enormous. In 1998, the IMF concluded that tax incentives had not been successful in attracting investment, especially foreign direct investment.¹³ At the same time, tax incentives have imposed serious costs on developing countries that need to be considered relative to any modest benefits they have created. Tax incentives by their nature represent a revenue cost for the government. For the most part, this revenue cost is wasted because the incentives go to investments that would have been made in any event. In other words, the expected benefits from foreign investment are outweighed by the lost income tax as a result of the tax breaks. There are various reasons why countries still apply tax incentives, including the pressure they get from multinational companies that threaten to locate elsewhere if they are not given concessions. A study of 40 Latin American, Caribbean and African countries for the period

10 Holland & Vann, “Income tax incentives for investment”, in *Tax Law Design and Drafting* (volume 2; International Monetary Fund: 1998; Victor Thuronyi, Ed.), <<https://www.imf.org/external/pubs/nft/1998/tlaw/eng/ch23.pdf>> (10 February 2015).

11 ActionAid, “Give us a break: How big companies are getting tax-free deals,” 2013, <http://www.actionaid.org/sites/files/actionaid/give_us_a_break_-_how_big_companies_are_getting_tax-free_deals_2.pdf> (15 July 2015).

12 ActionAid, “Responsible tax practice by companies”, 2015, <http://www.actionaid.org.uk/sites/default/files/publications/responsible_tax_practice.pdf> (15 July 2015).

13 Op. cit., Holland & Vann, 1998, p.3.

1985 to 2004 showed no benefit for total investment or economic growth as a result of tax incentives.¹⁴ Similarly, an empirical study of 12 west and central African countries over the period 1994-2006 showed no beneficial relationship between tax holidays and investment.¹⁵

According to the IMF, an important question is how to deal with the issue of depreciation during the holiday period. Should depreciation of equipment or machinery be deducted during the period or can this be deferred until after the holiday has terminated? Depreciation represents a cost in the calculation of income, and so its deduction is necessary to accurately measure the amount of income that should be subject to the holiday. Allowing a deferral of the deduction effectively overestimates the costs associated with the post-holiday period and so leads to a further reduction in tax, which can result in an even greater tax incentive.¹⁶

Increasing domestic revenues

In more recent years, the shift away from tax incentives has increased as part of wider discussions on how to increase domestic revenues. For instance, at an international conference organised by the IMF in March 2011 in Kenya, it was concluded that African nations need to re-examine their own tax systems and remove tax exemptions and inherent inefficiencies in those systems in order to raise revenues and fund development.¹⁷ In the same year the importance of addressing the governance of tax incentives was raised by the IMF, OECD, UN and World Bank in their joint report to the G20 on supporting effective tax systems in developing countries.¹⁸ In 2014, the OECD developed principles to enhance the transparency and governance of tax incentives for investment in developing countries. According to the OECD, there is strong evidence that calls into question the effectiveness of some tax incentives for investment, including in particular tax free zones and tax holidays. Ineffective tax incentives are no compensation for, or alternative to, a poor investment climate – in fact they may actually damage a developing country's revenue base by eroding resources for the real drivers of investment, namely infrastructure, education and security.¹⁹ And for natural resource exploitation in particular, tax breaks do not necessarily stimulate foreign investment, since these companies are specifically interested in the natural resources and cannot just pack up and move to another country as they could in the case of manufacturing. However, in practice, tax breaks are still abundantly provided.²⁰

This research paper takes a closer look at an excessively generous tax holiday awarded to NLNG, a joint venture company producing liquefied natural gas (LNG) in Nigeria of which Shell, Total and Eni are 51% shareholders.

14 OECD, "Tax and development – Draft principles to enhance the transparency and governance of tax incentives for investment in developing countries", 2014, <<http://www.oecd.org/ctp/tax-global/transparency-and-governance-principles.pdf>> (10 February 2015).

15 Op. cit., OECD 2014, p.1.

16 Op. cit., OECD 2014, p.1.

17 Taxation Info News, 2011, Remove tax exemptions in Africa, says IMF; <<http://www.taxationinfonews.com/2011/03/remove-tax-exemptions-in-africa-says-imf/#ixzz2CBv9aH49>> (15 July 2015).

18 Op. cit., OECD, 2014, p.2.

19 Op. cit., OECD, 2014, p.1.

20 See for instance Tax Justice Network-Africa and ActionAid International, "Tax competition in East Africa: A race to the bottom?", 2012, <http://www.actionaid.org/sites/files/actionaid/eac_report.pdf> (15 July 2015).

2. The foreign shareholders of NLNG: Royal Dutch Shell, Total and Eni

This chapter briefly introduces the three multinationals with a share in NLNG: Royal Dutch Shell, Total and Eni, with special attention to their policies on tax and transparency, as well as the companies' activities in Nigeria.

2.1 Royal Dutch Shell

General information (all figures for 2014)



Name	Royal Dutch Shell
Headquarters	The Netherlands/United Kingdom ²¹
Website	www.shell.com
Major products and services	Extraction of oil and natural gas, oil refining, energy distribution and sales
Turnover	US\$ 421.1 billion
Profit before tax	US\$ 28.3 billion
Total tax paid	US\$ 13.6 billion
Profit after tax	US\$ 14.7 billion
Number of subsidiaries	834
Employees	94,000 (worldwide)

Source: Shell Annual Report 2014, <http://reports.shell.com/annual-report/2014/servicepages/welcome.php>;

Subsidiaries from Orbis database, Sept 2014

Note: All figures are for 2014 and in billions of US\$ (consolidated figures)

Global activities

Royal Dutch Shell is a global group of energy and petrochemical companies, with operations in more than 70 countries and territories. The company has strong operational performance and productive investments in Australia, Brazil, Brunei, Canada, China, Denmark, Germany, Malaysia, the Netherlands, Nigeria, Norway, Oman, Qatar, Russia, the UK and the USA. It has major interests in Africa, with a

²¹ The parent company Royal Dutch Shell plc is incorporated in England and Wales, and headquartered and resident in the Netherlands; Shell Annual Report 2014.

focus on Nigeria, Egypt, Gabon and South Africa. The company produces 3.1 million barrels of oil equivalent every day. Shell has interests in 24 refineries and chemical plants worldwide.²²

Liquefied natural gas (LNG) activities

According to its website, Shell helped pioneer the LNG sector, providing the technology for the world's first commercial liquefaction plant at Arzew, Algeria, in 1964. The company has LNG supply projects – either in operation or under construction – in seven countries, including NLNG in Nigeria. Shell has major interests in one regasification plant (Hazira, India), and long-term access to capacity in several others in Europe, the Middle East and North America.²³ Shell sold 24 million tonnes of LNG in 2013.²⁴

Corporate structure

The parent company Royal Dutch Shell plc²⁵ is incorporated in England and Wales, and headquartered and resident in the Netherlands for Dutch and UK tax purposes.²⁶ Royal Dutch Shell plc is listed on the London, Amsterdam, and New York stock exchanges. In 2014, Royal Dutch Shell was ranked as the second largest multinational corporation worldwide in the Global Fortune 500 (after having been no. 1 for two years).²⁷ Shell is one of the world's five largest private oil and gas companies, a group also known as the 'supermajors'.²⁸

Financial transparency and tax governance

In recent years, Shell has made considerable improvements in terms of financial transparency. Most notably, since 2012 Shell has published an annual overview of payments made to governments in some of the main countries where it operates. In this annual statement, Shell discloses how much it paid to 14 host governments, including Nigeria.²⁹ In 2014, the company paid globally US\$ 14.3 billion in corporate taxes³⁰, and US\$ 3.9 billion in royalties. The company adds that it collected US\$ 72.7 billion in excise duties and sales taxes on fuel and other products on behalf of governments. According to its Annual Report, Shell's effective tax rate in 2014 was 48%.³¹

Earlier SOMO research showed that this relatively high effective tax rate for Shell (and other oil companies) can be explained by the typical structure of the oil and gas industry. A distinction should

22 Shell website, <<http://www.shell.com/global/aboutshell/at-a-glance.html>> (15 July 2015).

23 Shell website <<http://www.shell.com/global/future-energy/natural-gas/liquefied-natural-gas/projects.html>> (15 July 2015).

24 Shell website <<http://reports.shell.com/annual-report/2014/strategic-report/upstream.php>> (15 July 2015).

25 In this report, whenever the abbreviation 'Shell' is used, it refers to the parent company Royal Dutch Shell plc.

26 K. Sluyterman, "Keeping competitive in turbulent markets, 1973–2007: A History of Royal Dutch Shell", 2007, p.5.

27 Fortune website <<http://fortune.com/global500/2014/royal-dutch-shell-2/?iid=lefttrail>> (26 Jan 2015).

28 The supermajors are considered to be BP plc, Chevron Corporation, ExxonMobil Corporation, Royal Dutch Shell plc and Total SA, <http://en.wikipedia.org/wiki/Big_Oil#cite_note-reut1808-1> (26 Jan 2015).

29 Shell website <<http://s00.static-shell.com/content/dam/shell-new/local/corporate/corporate/downloads/pdf/payments-to-governments-brochure-2014.pdf>> (15 July 2015).

30 This figure differs from the amount reported in the table above, which is explained as follows: the amount of taxes paid (US\$ 14.3 billion) is taken from the cash flow statement (actually paid taxes in 2014), while the total tax paid as reported in the table (US\$ 13.6 billion) refers to the amount of tax booked in the income statement (taxation booked over 2014).

31 This figure is calculated as follows: total tax expenses / income before taxation = 13,584 million. / 28,314 million. = 48.0%. Shell Annual Report 2014, p.127. A generally accepted formula for calculation of the effective tax rate can be found here: <<http://www.investopedia.com/terms/e/effectivetaxrate.asp>> (15 July 2015).

be made between tax paid for upstream activities (in countries of production) and for downstream activities (in countries where the oil is processed and marketed). The tax rate for upstream activities is generally much higher than in most other industries because of royalties paid over the oil produced. This gives the impression that the effective tax rate is higher than average, even though the oil industry's tax payments are not comparable to other sectors of the economy that are paying corporate income tax only and – with the exception of mining companies – do not pay royalties as they do not extract any resources.³²

According to Shell, *"Tax binds governments, communities and businesses together. Revenue transparency provides citizens with an important tool to hold their government representatives accountable and to advance good governance. Shell is committed to transparency as it builds trust. Trust is essential for a company that operates in our line of business, reflecting our core values of honesty, integrity and respect for people. This is the fourth consecutive year that Shell is publishing the revenues that its operations generate through income taxes, royalties and indirect taxes for governments around the world. In 2014, this amounted to over US\$ 90 billion. To put it in perspective, this equates to over half the 2014 budget of the European Union. We have been publishing payments to governments voluntarily, because for Shell, paying taxes in the countries where we operate is more than complying with the law; it is about showing that extraction of natural resources leads to the opportunity of government revenue, economic growth and social development."*³³

In the same report, it is also stated that *"Shell supports predictable and stable tax regimes that incentivise long term investment. Next year, following the transposition of the 2013 EU Accounting and Transparency Directives into UK law, we will report our payments to governments pursuant to the UK's Reports on Payments to Governments Regulations 2014."*³⁴ These new disclosure regulations may put companies like Shell in the difficult situation of breaking the law in certain host countries by complying with the UK law, or breaking the law in the UK by not reporting on those host countries. *We continue to consult several governments on this matter, including the UK. We also engage with host governments and joint venture partners to explain our new reporting obligations."*³⁵

Although this step is an important improvement on earlier years, it is still a long way from full financial transparency. In response to Shell's 2014 'payments to governments' overview, Tax Justice Netherlands called on Shell to be truly transparent about its tax payments to governments. According to Tax Justice Netherlands, the tax figures provided are too limited to be meaningful, give a biased

32 For the period 2007 to 2009, SOMO calculated an average upstream tax rate for Shell of 48.5%. In the same period, the average tax rate for downstream (e.g. refining, distribution and marketing activities for oil products and chemicals) and corporate (holdings and treasury, headquarters, central functions and Shell's insurance activities) activities on the other hand was only 7.6%. This calculation has not been repeated for the current situation, but it is likely that the numbers will be in the same order of magnitude; SOMO, 2009, Royal Dutch Shell – Overview of controversial business practices in 2009; <http://www.somo.nl/publications-en/Publication_3481> (15 July 2015).

33 Shell, 2015, "Payments to governments – revenue transparency," <<http://s00.static-shell.com/content/dam/shell-new/local/corporate/corporate/downloads/pdf/payments-to-governments-brochure-2014.pdf>> (15 July 2015).

34 For more info about the EU Accounting and Transparency Directive, see: CCFD-Terre Solidaire, 2013, Country by country transparency: Dodd Frank act and EU Directives, <http://www.oecd.org/ctp/tax-global/Country_by_country_transparency-DoddFrankAct_and_EUDirectives.pdf> (1 April 2015).

35 Op. cit., Shell, 2015.

view of the company's own tax payments as it includes excise duties and sales taxes, and some of the figures provided are unclear and/or incomplete.³⁶

Shell's activities in Nigeria

Shell has been active in Nigeria since the 1930s. Shell first entered Nigeria through a joint venture with Anglo-Persian (later renamed BP) during the 1930s, when the country was still a British colony. In 1956 the joint venture discovered oil in commercial quantities in the Niger Delta, which signalled the start of large-scale oil production.³⁷

The main business of Shell in Nigeria includes onshore and offshore oil production and natural gas production.³⁸ Shell's share of production (onshore and offshore) in Nigeria was approximately 300,000 barrels of oil equivalent per day (boe/d) in 2014, compared with approximately 265,000 boe/d in 2013. Security issues and crude oil theft in the Niger delta continued to be significant challenges in 2014.³⁹

In relation to gas production, Shell has a 25.6% interest in NLNG. According to its website it operates NLNG, describing it as "*Nigeria's largest liquefied natural gas (LNG) plant, which exports all over the world.*"⁴⁰ Another subsidiary, Shell Nigeria Gas (SNG), was incorporated in 1998 for the downstream distribution of gas to industry in Nigeria. Shell currently produces about 70% of Nigeria's gas supply. Shell's natural gas production in Nigeria in 2014 amounted to 791 million standard cubic feet (SCF) per day in Nigeria. In 2014, LNG production was higher than in 2013, as 2013 was impacted by gas supply constraints and the impact of a blockade of NLNG export facilities by the Nigerian Maritime Administration and Safety Agency (NIMASA).⁴¹

There is a lot of publicly available information regarding Shell's tax payments to the Nigerian government, including data from Shell's website, the Nigerian EITI and the annual accounts of some of Shell's subsidiaries. In its overview of tax payments to governments, Shell reports that in 2014 it paid US\$ 2.3 billion income tax and US\$ 727 million in royalties to the Nigerian government, totalling around US\$ 3 billion.⁴²

The response by Shell to the draft findings can be found in Annex 4.

36 Reaction of Tax Justice NL to Shell's tax reporting: not nearly adequate, <<http://www.taxjustice.nl/publications/reaction-of-tax-justice-nl-to-shells-tax-reporting-not-nearly-adequate/>> (14 Jan 2016).

37 Op. cit., K. Sluyterman, p.343–349.

38 Shell Nigeria website <http://www.shell.com.ng/home/content/nga/aboutshell/at_a_glance/> (15 July 2015).

39 Shell, "Investor's Handbook 2014," p.21, <http://reports.shell.com/investors-handbook/2014/servicepages/downloads/files/entire_shell_ih14.pdf> (15 July 2015).

40 Shell website, <<https://www.shell.com.ng/aboutshell/who-we-are.html>> (22 July 2015).

41 Shell, "Investor's Handbook 2014," p.21.

42 Op. cit., Shell, 2015.

2.2 Total

General information (all figures for 2014)



Name	Total
Headquarters	France
Website	www.total.com
Major products and services	International oil company and natural gas operator, refiner, petrochemical producer and fuel and lubricant retailer
Turnover	US\$ 212.0 billion
Profit before tax	US\$ 12.9 billion
Total tax paid	US\$ 8.6 billion
Profit after tax	US\$ 4.3 billion
Number of subsidiaries	898
Employees	100,000 (worldwide)

Source: Total Annual Report Form 20F 2014, http://www.total.com/sites/default/files/atoms/files/form_20-f_0.pdf

Note: All figures are for 2014 and in billions of US\$ (consolidated figures)

Global activities

Total describes itself as *"a leading international oil and gas company, producing, refining and marketing oil and manufacturing petrochemicals, and a major player in natural gas and solar energy."*⁴³ In 2014, average daily oil and gas production was 2.1 million boe/d (barrels of oil equivalent/day). Of this total production, 20% consists of LNG.⁴⁴ With operations in more than 130 countries, Total is engaged in every sector of the oil industry, including upstream (hydrocarbon exploration, development and production) and downstream (refining, petrochemicals, specialty chemicals, trading and shipping of crude oil and petroleum products, and marketing). Total also operates in the power generation and renewable energy sectors.⁴⁵

LNG activities

According to its website, *"Total is a pioneer and global leader in LNG, a strategic sector for us. We are active in the upstream and midstream of the LNG value chain and are cementing our positions in most major producing regions and consumer markets."*⁴⁶ Also, it states that *"With interests in 10 liquefaction complexes already in operation and involved in a number*

43 Total website, <<http://www.total.com/en/corporate-profile/thumbnail/total-glance-fourth-largest-global-oil-and-gas-company-1>> (15 July 2015).

44 Total website, <<http://www.total.com/en/corporate-profile/thumbnail/totals-key-figures>> (15 July 2015).

45 Total Annual Report 2014, <http://www.total.com/sites/default/files/atoms/files/form_20-f_0.pdf> (22 July 2015).

46 Total website, <<http://www.total.com/en/about-total/organization/business-segments/upstream/gas-power>> (26 Jan 2015).

of projects under construction or in the planning stages, Total is heavily committed to LNG. Backed by our 50 years of experience and a strategy geared to the long term, we will support the growth of this industry."⁴⁷ Total claims to be the second-ranking operator in the international LNG industry. Total's LNG production in 2014 was 12 million tons.

Corporate structure

Total S.A. is a *société anonyme* (limited company) incorporated in France in 1924 and listed on the Paris, Brussels, London and New York stock exchanges. In 1999, the company acquired PetroFina S.A. and, in 2000, acquired Elf Aquitaine S.A.⁴⁸ In 2014, Total was ranked as the 11th largest multinational corporation worldwide in the Global Fortune 500.⁴⁹ Total is one of the world's five largest private oil and gas companies, a group also known as the 'supermajors'.⁵⁰

Financial transparency and tax governance

Total has developed a one page tax policy which states, among other things, that *"Tax payments of TOTAL represent a substantial part of our group's economic contribution to the countries in which we operate. While it is generally acknowledged that the prime objective of tax systems is to yield tax revenue, fair and stable tax policies are required in the longer term to encourage business investments. This is particularly true for the oil and gas industry, which is capital intensive, high risk and long term. We strongly believe in the investment dynamic created by a stable, clear and equitable fiscal regime which will encourage sustainable future development. TOTAL is mindful of its responsibility and is committed to paying its fair share of taxes to the countries in which it operates, in compliance with applicable laws and conventions and in accordance with our Code of Conduct and Code of Ethics."* The policy continues by stating that *"While we fully support initiatives for greater transparency and accountability, such as the EITI, we would encourage the regulators to ensure that initiatives are consistent, coordinated and proportionate in the tax reporting obligations they will impose upon multinational groups."*⁵¹

On its website it states that *"Total is committed to strict transparency concerning the revenues generated by our activities and we participate actively in intergovernmental initiatives and dialogue on this issue."*⁵² This includes Total's commitment to the EITI by promoting EITI principles to its host countries and helping them put the principles into practice. On its website, Total states that *"In addition to supporting the EITI, we publish detailed reports on several host countries where we have significant production activities. These seven countries accounted for 47% of the Group's production in 2013. These reports provide information on:*

47 Total website, <<http://www.total.com/en/energies-expertise/oil-gas/exploration-production/strategic-sectors/lng/total-world-class-player>> (26 Jan 2015).

48 Op. cit., Total Annual Report 2014.

49 Fortune website, <<http://fortune.com/global500/2014/total-11/?iid=lefttrail>> (15 July 2015).

50 The supermajors are considered to be BP plc, Chevron Corporation, ExxonMobil Corporation, Royal Dutch Shell plc and Total SA, <http://en.wikipedia.org/wiki/Big_Oil#cite_note-reut1808-1> (15 July 2015).

51 Total website, <<http://www.total.com/sites/default/files/atoms/file/tax-policy>> (15 July 2015).

52 Total website, <<http://www.total.com/en/society-environment/ethics-and-values/areas-focus/promoting-financial-transparency-0?xtmc=transparency&xtnp=1&xtcr=1>> (15 July 2015).

- ❑ The extent of our acreage.
- ❑ The types of contracts held.
- ❑ The activities of our affiliates.
- ❑ The taxes paid to the government.

We also publish information each year about our oil and gas exploration and production activities, broken down by country, in our *Total Factbook 2013*.⁵³ According to Total's Chief Financial Officer, "Total's overall tax rate is 56%, far higher than the French tax rate of 34%. It varies by host country – we operate in 130 – and by business. It can be as high as 85% for profits related to oil and gas production and as low as 30 to 35% for refining, marketing and chemicals."⁵³ As explained in Chapter 2.1, this figure gives the impression that the effective tax rate of Total is higher than average, even though the oil industry's tax payments are not comparable to other sectors of the economy.

Based on publicly available information and compared to other oil companies Total appears not to be a frontrunner in terms of financial transparency. The *Factbook 2013*, which the company suggests reports on a country-by-country basis, includes no financial information on a country-by-country basis. The company published seven country reports (Angola, Gabon, Republic of Congo, Indonesia, Nigeria, Norway and UK), but these reports provide only very limited information on taxes paid to the governments⁵⁴ and in the case of Angola there is no information on taxes paid at all, stating "Angola has decided not to pursue the implementation of EITI."⁵⁵

Total's activities in Nigeria

According to the company's Annual Report 2013, Total's production in Nigeria in 2014 was 257,000 boe/d compared to 261,000 boe/d in 2013. This drop was primarily due to the sharp increase in illegal oil bunkering (stealing of oil) and a blockade of NLNG's export cargos in 2013. Nigeria is the leading contributor to Total's production. Total, which has been present in the country since 1962, is the operator of five production licences (OML), while it holds interests in a further 32 production licences, as well as in four oil prospecting licences (OPL).⁵⁶

Total is also active in the LNG sector through its 15% stake in NLNG. In addition, TOTAL holds a 20.48% stake in Brass LNG, which is carrying out scoping studies for the establishment of a large gas liquefaction plant.⁵⁷

In a separate report on Nigeria, Total reports a total amount of taxes paid to the Nigerian government of US\$ 1.7 billion in 2013 consisting of taxes and royalties, as can be seen in Table 1. In addition to the above taxes and royalties, the Federal government also received 5,268 million Naira

53 Total website, <<http://www.total.com/en/media/news/news/20110415-does-total-pay-income-tax-france-patrick-chevardiere-answers?xtmc=tax&xtnp=1&xtr=1>> (26 Jan 2015).

54 Total website, <http://www.total.com/en/media/publications?field_publication_category_tid_i18n=434> (15 July 2015).

55 Total website, <<http://www.total.com/sites/default/files/atoms/files/fiche-itie-angola-en-2013.pdf>> (26 Jan 2015).

56 Total Annual Report 2014.

57 Total Annual Report 2014.

(or app. US\$ 26.5 million) in 2013 as Niger Delta Development Commission contributions for Total’s oil operations in Nigeria.⁵⁸

Table 1: Taxes paid to the Nigerian government by Total

Millions US\$	2013	2014
Petroleum profit tax	698	1,053
Royalty - oil	624	796
Royalty - gas	37	35
Other taxes	334	322
Total	1,693	2,206

Source: Total, 2014, Financial Transparency – Example of Total in Nigeria

In its 2014 Annual Report, Total states that “the Nigerian government has been contemplating new legislation to govern the petroleum industry which, if passed into law, could have an impact on the existing and future activities of the Group in that country through increased taxes and/or costs of operation and could adversely affect financial returns from projects in that country.”⁵⁹

The response by Total to the draft findings can be found in Annex 4.

58 Total, “Financial transparency – Example of Total in Nigeria,” 2014, <http://www.total.com/sites/default/files/atoms/files/fiche-itie-nigeria-en-2013_0.pdf> (15 July 2015).

59 Total Annual Report 2014.

2.3 Eni

General information (all figures for 2014)⁶⁰



Name	Eni
Headquarters	Italy
Website	www.eni.com
Major products and services	Integrated energy company, committed to finding, producing, transporting, transforming and marketing oil and gas
Turnover	US\$ 134.0 billion
Profit before tax	US\$ 8.9 billion
Total tax paid	US\$ 7.9 billion
Profit after tax	US\$ 1.0 billion
Number of subsidiaries	269
Employees	84,405 (worldwide)

Source: Eni Annual Report 2014,

https://www.eni.com/en_IT/attachments/publications/reports/reports-2014/Integrated-Annual-Report-2014.pdf

Note: All figures are for 2014 and in billions of US dollars (consolidated figures)

Global activities

Eni is an integrated company that operates across the entire energy chain, employing more than 84,000 people in 83 countries around the world, active in exploration and production, gas and power generation, and refining and marketing. For the year 2014, Eni's production of oil and natural gas was 1.6 million boe/day.⁶¹

LNG activities

Eni is engaged at all stages of the gas value chain: supply, trading and marketing of gas and electricity, gas infrastructure, and LNG supply and marketing. Eni sells more than 60% of its gas outside Italy and it has a leading position in the European gas market.⁶² In 2014, LNG sales (13.3 bcm) increased by 0.9 bcm from 2013. In particular, LNG sales of the Gas & Power segment

⁶⁰ Financial figures originally reported in Euros as follows: Turnover €109.8 billion, Profit before tax €7.3 billion, Total tax paid €6.5 billion, Profit after tax €850 million; conversion into US\$ based on annual average exchange rate of 1 US\$ = €0.8191; <<http://www.oanda.com/currency/historical-rates/>>.

⁶¹ Eni website, <http://www.eni.com/en_IT/attachments/azienda/profilo-compagnia/eni_sintesi_eng.pdf> (15 July 2015).

⁶² Eni website, <http://www.eni.com/en_IT/attachments/azienda/profilo-compagnia/eni_sintesi_eng.pdf> (15 July 2015).

(8.9 bcm, included in worldwide gas sales) mainly concerned LNG from Qatar, Algeria and Nigeria marketed in Europe, South America and the Far East.⁶³

Corporate structure

Eni is 70% owned by private shareholders (including the People's Bank of China's 2.1% share) and 30% by the Italian government (4.3% by the Ministry of Economy and Finance, 25.7% by Cassa Depositi e Prestiti S.p.A. (CDP S.p.A.)).⁶⁴ Eni's shares are listed on the Milan and New York Stock Exchanges.⁶⁵ In 2014, Eni was ranked as the 22nd largest multinational corporation worldwide in the Global Fortune 500.⁶⁶

Financial transparency and tax governance

According to its website *"Eni is an integrated company which interacts continuously with its stakeholders. The clear and transparent dialogue with each of them is an important aspect of the company's operating way, since it enables Eni to establish constructive relationships aimed at making its business activities ever more solid while creating sustainable value for all the stakeholders."*

It continues by saying that *"At the country subsidiary level, Eni is promoting reporting procedures for sustainability issues, including country reports, along with the sustainability reports of subsidiaries operating in specific businesses such as power generation and gas."*⁶⁷

On a positive note, in its Annual Report and on its website Eni publishes an overview of investments and revenues for 14 countries, including both EITI and non-EITI subscribing countries of producing countries that subscribe to the EITI. During Eni's Annual Shareholders Meeting in 2014, Eni answered to a number of questions raised by the Italian NGO Fondazione Culturale Responsabilità Etica (Fcre). Already in 2009, the company committed itself to reducing the presence of the company's subsidiaries in tax havens or opaque financial jurisdictions at the request of the same NGO, and based on the answers provided by Eni, it can be concluded that the company is relatively transparent compared to other major oil companies. In an extensive 214-page document the company provides clarification on the presence of some of its subsidiaries in tax havens, and detailed information about its tax policies.⁶⁸

63 Eni Annual Report 2014.

64 Eni website, http://www.eni.com/en_IT/governance/shareholders/relevant-participation/relevant-participation.shtml (15 July 2015).

65 Eni website, http://www.eni.com/en_IT/investor-relation/eni-stock-markets/eni-stock.shtml (15 July 2015).

66 Fortune website, <http://fortune.com/global500/eni-22/> (15 July 2015).

67 Eni website, http://www.eni.com/en_IT/sustainability/reporting-system/reporting-system.shtml (15 July 2015); http://www.eni.com/en_IT/sustainability/the-fight-against-corruption/fac-transparency-payments/transparency-payments.shtml (30 September 2015).

68 Eni, Answers to the questions received prior to the Shareholders' Meeting 2014, pursuant to art.127-ter of Italian Legislative Decree n. 58/19981, 2014, http://www.eni.com/en_IT/attachments/governance/shareholder-meeting/2014/Q&A_Eng-2014.pdf (15 July 2015).

Eni's activities in Nigeria⁶⁹

Eni has been established in Nigeria for several decades and is involved in various Nigerian oil and natural gas projects. In 2014, total production in Nigeria was 135,000 boe/d, increasing from 125,000 boe/d in 2013.⁷⁰ Eni holds a 10.4% interest in the Nigeria LNG Ltd joint venture.⁷¹

In Eni's overview of payments made to the Nigerian government, it was reported that in 2014, profit taxes⁷² amounted to US\$ 313 million, royalties US\$ 295 million and other significant benefits to government of US\$ 32 million.⁷³

The response by Eni to the draft findings can be found in Annex 4.

69 This section is shorter than the sections on Shell and Total in Nigeria because only limited information is available.

70 Eni Annual Report 2014.

71 Eni Annual Report 2014.

72 This includes corporate tax-other tax on income/profit or production, e.g. petroleum revenue tax.

73 Eni Annual Report 2014. Based on annual average exchange rate of 1US\$ = €0.8191 as provided by email by Eni (30 September 2015).

3 The oil and gas industry in Nigeria

This chapter provides an introduction to the oil and gas industry in Nigeria and to the Nigerian tax system as it relates to oil and gas. It also provides a summary of the developments around financial transparency in the oil and gas sector in Nigeria.

3.1 Nigeria's oil and gas industry

Nigeria's natural resource wealth includes both oil and natural gas. The country produces 25% of all African crude oil and 3% of the world total, and is a member of the Organization of Petroleum Exporting Countries (OPEC).⁷⁴ In 2014, total Nigerian oil production averaged 2.4 million barrels per day.⁷⁵ Nigeria is the largest oil producer in Africa and the world's 10th largest oil producer and the country is among the world's top five exporters of LNG.⁷⁶ Despite the relatively large volumes of oil it produces, Nigeria's oil production is hampered by instability and supply disruptions, while the natural gas sector is restricted by the lack of infrastructure to monetize natural gas that is currently flared (burned off).⁷⁷

Oil in Nigeria

The petroleum sector in Nigeria has typically in the past few years (though this fluctuates) accounted for about 80% of fiscal revenues (the share of oil industry taxes in total tax revenues); 90–95% of export revenues (share of export revenues from oil in total export revenues); and 30–35% of GDP. Oil revenues are divided between the three tiers of government: federal, state and local. The federal government typically gets about half of revenues; the 36 state governments about a quarter; and the 774 local governments about a fifth. The rest flows to special funds including the Niger Delta Development Commission.⁷⁸

Despite earning more than US\$ 400 billion in revenue from oil since the early 1970s, Nigeria is still considered a lower-middle income country, with GDP per capita of US\$ 3,185 (2014).⁷⁹ The vast majority of its 178.5 million citizens have seen little benefit from this legacy of oil and gas wealth.⁸⁰ The population living below the poverty line (below US\$ 1.25 per day) was 62% in 2010, slightly up from 61.8% in 2004.⁸¹ In 2013, Nigeria ranked 152 out of 187 in the UN Human Development

74 Natural Resource Governance Institute website, <<http://www.resourcegovernance.org/countries/africa/nigeria/extractive-industries>> (15 July 2015).

75 US Energy Information Administration website: <http://www.eia.gov/beta/international/country.cfm?iso=NGA> (15 July 2015).

76 Natural Resource Governance Institute website, <<http://www.resourcegovernance.org/countries/africa/nigeria/overview>> (15 July 2015).

77 Ibid.

78 N. Shaxson, "Nigeria's Extractive Industries Transparency Initiative – just a glorious audit?" November 2009, Chatham House, London.

79 World Bank website, <<http://data.worldbank.org/indicator/NY.GDP.PCAP.CD>> (15 July 2015).

80 World Bank website, <<http://data.worldbank.org/country/nigeria>> (15 July 2015).

81 MDG Indicators website, <<http://mdgs.un.org/unsd/mdg/SeriesDetail.aspx?srid=580>> (15 July 2015).

Index.⁸² The World Bank reported in 2014 that Nigeria is home to 7% of the world's extreme poor, and that it ranks third among the countries with the highest population of extreme poor or people with abject poverty in the world, after India (with 33% of the world's poor) and China (13%).⁸³

Major international players

The major international players in Nigeria's oil and natural gas sectors are Shell, ExxonMobil, Chevron, Total and Eni. Six joint venture arrangements dominate oil production in Nigeria. Government, acting through the national oil company, controls a majority share and Shell, Chevron, Mobil, Agip, Elf and Texaco serve as minority shareholders and operators in all oil operations in Nigeria. In recent years, the government has struggled to fulfill its financial contributions to these arrangements, forcing it to take out oil-backed debts from the operating partners and impeding investment in the jointly controlled assets.⁸⁴ International Oil Companies (IOCs) participating in onshore and shallow water oil projects in the Niger delta region have been affected by instability in the region. As a result, there has been a general trend for IOCs, particularly Shell, Total, Eni, Chevron, and ConocoPhillips, to sell their interests in marginal onshore and shallow water oil fields, mostly to Nigerian companies and smaller IOCs, and to focus their investments on deep-water projects and onshore natural gas projects.⁸⁵

While joint ventures control the largest producing areas, offshore production is rising after several large finds, including Shell's Bonga field and Chevron's Agbami field. These and other offshore assets are governed by production sharing contracts (PSCs) that will account for an increasing share of production in coming years. The fiscal terms of the PSCs will give the government a significantly smaller take per barrel than they currently get through the joint ventures. This has significant implications for revenues should PSC production continue to grow faster than joint venture production.⁸⁶

Natural gas in Nigeria

Nigeria is not only rich in oil but also in natural gas. It is the largest holder of proven natural gas reserves in Africa and the ninth largest holder in the world. Nigeria produced 1.35 trillion cubic feet (Tcf) of dry natural gas⁸⁷ in 2013, ranking among the world's top 30 largest natural gas producers.

82 UNDP, 2014, Human Development Report 2014 – Nigeria, <http://hdr.undp.org/sites/all/themes/hdr_theme/country-notes/NGA.pdf> (15 July 2015).

83 World Bank, "Prosperity for All / Ending Extreme Poverty: A note for the World Bank Group Spring Meetings 2014," 2014, <http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1327948020811/8401693-1397074077765/Prosperity_for_All_Final_2014.pdf> (8 April 2015).

84 Natural Resource Governance Institute website, <<http://www.resourcegovernance.org/countries/africa/nigeria/extractive-industries>> (15 July 2015).

85 US Energy Information Administration website, <<http://www.eia.gov/beta/international/analysis.cfm?iso=NGA>> (26 Jan 2015).

86 Natural Resource Governance Institute website, <<http://www.resourcegovernance.org/countries/africa/nigeria/extractive-industries>> (26 Jan 2015).

87 Dry natural gas is natural gas which remains after: 1) the liquefiable hydrocarbon portion has been removed from the gas stream (i.e., gas after lease, field, and/or plant separation); and 2) any volumes of nonhydrocarbon gases have been removed where they occur in sufficient quantity to render the gas unmarketable. Note: Dry natural gas is also known as consumer-grade natural gas; <<http://www.eia.gov/tools/glossary/?id=natural%20gas>> (15 July 2015).

Box 2: Gas flaring in Nigeria

A significant amount of Nigeria's gross natural gas production is flared (burned off) because some of Nigeria's oil fields lack the infrastructure needed to capture the natural gas that is a by-product of oil, known as associated gas (AG). Since the 1990s there has been wide agreement that continuous flaring of associated gas must be stopped. In 2013, Nigeria flared 428 Bcf of its associated gas production, or 15% of its gross production. This is a significant decrease compared to 2010, when 540 Bcf was flared. According to the US National Oceanic and Atmospheric Administration (NOAA), natural gas flared in Nigeria accounted for 10% of the total amount flared globally in 2011.¹

In 2008, the Nigerian government developed a Gas Master Plan that promoted investment in pipeline infrastructure and new gas-fired power plants to help reduce gas flaring and generate much-needed electricity. However, progress is still limited as security risks in the Niger Delta have made it difficult for international oil companies to construct infrastructure that would support the capture and sale of associated gas.² According to Shell, one of the largest gas producers in the country, the impediments to decreasing gas flaring have been the security situation in Niger Delta and the lack of partner funding that has slowed progress on projects to utilize associated gas. The company recently reported that it was able to reduce the amount of gas it flared in 2012 because of improved security in some Niger Delta areas and stable co-funding from partners, which allowed Shell to install new gas-gathering facilities and repair existing facilities damaged during the civil crisis of 2006 to 2009.³

However, civil society organisations have been critical of the implementation of gas flaring regulations in Nigeria. In 2011, Friends of the Earth Nigeria reported that *"several unsuccessful attempts at stopping gas flaring in Nigeria due mainly to the failure of the Nigerian government to enforce existing legislations and the deceptive resort to a policy of imposing non-binding gas flare out deadlines which were continually moved as the deadline approached."*⁴ A report by the Petroleum Revenue Special Task Force in 2012 found that oil companies often do not pay fines, and that the Nigerian Oil Ministry is unable to independently track and measure gas volumes produced and flared as this depends largely on information provided by operators.⁵ Up to now, continuous gas flaring is leading to enormous environmental and economic losses. In 2015, according to a Nigerian newspaper, *"Nigeria's revenue dips by at least US \$800 million annually due to continuous gas flaring in the country."*⁶

1 US Energy Information Administration website, <<http://www.eia.gov/beta/international/analysis.cfm?iso=NGA>> (15 July 2015).

2 Ibid.

3 Ibid.

4 Environmental Rights Action/ Friends of the Earth Nigeria, 2011, "Mired in a fossil trap – the Nigerian CDM report: <<http://eraction.org/publications/Mired%20in%20Fossil%20Trap.pdf>> (15 July 2015).

5 Gas Flare Tracker website: <<http://gasflaretracker.ng/about.html>> (15 July 2015).

6 New Telegraph, "Nigeria loses \$800m annually to gas flaring," 2015, <<http://newtelegraphonline.com/146384/>> (15 July 2015).

In the past, much of the associated gas⁸⁸ was burned off because of insufficient local demand. However the flaring of gas was both considered a waste and also harmful to the environment (see Box 2). From the late 1960s, the Nigerian government and several oil companies, including Shell and BP, negotiated for a liquefied natural gas (LNG) scheme for Nigeria, including the Bonny Liquefied Natural Gas scheme launched in 1976.⁸⁹ This resulted in the setting up of Nigeria LNG Company (NLNG), which was incorporated in 1989. Various delays meant the final investment decision to build a liquefied natural gas plant was only signed in 1995, and operations started in 1999.⁹⁰ NLNG is described in more detail in Chapter 4.

Nigeria has the largest reserves of proven natural gas reserves in Africa, and in the world, with an estimated 180 trillion cubic feet (Tcf) of proved natural gas reserves as of January 2015 (the majority in the Niger Delta). In 2013 Nigeria produced 1.35 Tcf of dry natural gas, leading to its rank among the world's top 30 largest natural gas producers, though the natural gas industry is affected by the same security and regulatory issues that affect the oil industry.⁹¹

3.2 The tax system in the Nigerian oil and gas industry

Companies carrying out petroleum operations are taxed under the Petroleum Profits Tax Act (PPTA) 2004. Under this Act, there are four possible arrangements, and in each case, the Nigerian National Petroleum Corporation (NNPC) represents the Nigerian government.⁹² Nigeria operates both a licensing and a contractual regime.

Under the licensing regime, there are two arrangements:⁹³

- ❑ joint ventures between NNPC and an international oil company (IOC)⁹⁴
- ❑ joint ventures between NNPC and a sole risk operator (SRO)

Under the contractual regime, there are also two arrangements:

- ❑ risk service contracts (RSC)
- ❑ production sharing contracts (PSC)

A production sharing contract is an agreement between the state oil company, the NNPC, and any other exploration and production company. PSCs have recently become Nigeria's preferred choice in the exploration of petroleum resources over time, particularly for offshore fields. Under a PSC the

88 Associated natural gas is natural gas that occurs in crude oil reservoirs as free gas; <<http://www.eia.gov/tools/glossary/?id=natural%20gas>> (15 July 2015).

89 Total and Eni are not mentioned as initiators but that does not mean they were not involved at this stage; K. Sluyterman, "Keeping competitive in turbulent markets, 1973-2007 – A history of Royal Dutch Shell," 2007, p343–349.

90 Nigeria LNG, 2015, Facts and figures on NLNG 2015, p.23; <http://www.nlng.com/Media-Center/Publications/Facts_and_figures_2015.pdf> (15 July 2015).

91 See <<http://www.eia.gov/beta/international/analysis.cfm?iso=NGA>> (10 February 2015).

92 NNPC website, <<http://www.nnpcgroup.com/Home.aspx>> (22 July 2015).

93 Ernst & Young, 2015 Global oil and gas tax guide; <<http://www.ey.com/GL/en/Services/Tax/Global-oil-and-gas-tax-guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/GOG-2014/GOG-NG.xml>> (15 July 2015).

94 Most relevant for this report as NLNG falls under this type of arrangement.

contractor funds exploration and production activities and recovers the cost of winning crude oil. A PSC is based on a production split, shared between the parties in agreed proportions.⁹⁵

Types of taxes

There are different types of taxes in the oil and gas industry in Nigeria.⁹⁶ They are specified in two laws: the Companies Income Tax Act and the Petroleum Profit Tax Act. The following taxes are applicable to oil and gas companies

- ❑ **Income tax:**⁹⁷ Companies engaged in *petroleum operations* are subject to tax under the Petroleum Profit Tax Act. For oil companies operating in Nigeria, corporate income tax is called Petroleum Profit Tax. The applicable Petroleum Profit Tax (PPT) rate is 85% of the net sales of oil. A reduced rate of 65.75% (for the first five years of existence of a company) applies if certain conditions are met. However, for petroleum operations carried out under the PSC regime, the applicable rate is 50%. The profit is determined by taking the proceeds of sales of oil, minus a restricted list of expenditures made to produce this oil.⁹⁸ *Liquefied natural gas* is specifically excluded from the definition of 'petroleum' and therefore it is likely that it is also excluded from the definition of 'petroleum operations'. This means that a rate of 30% is applicable for LNG operations. This is confirmed by the Ernst & Young Worldwide Corporate Tax Guide for Nigeria, which states that companies engaged in gas exploration are subject to the Companies Income Tax Act and are thus charged at 30%.⁹⁹
- ❑ **Royalties:** Any company engaged in upstream oil operations is required to pay royalties in accordance with the provisions of the Petroleum Act and the Petroleum Drilling Regulations 2004. This is usually in the form of monthly cash payments at an agreed percentage of the quantity of oil produced, after making adjustments for treatment, handling and related expenses. The royalty payable is dependent on the concession agreement between the company and the government and is usually between 0–20%.¹⁰⁰ Royalties on gas are based on gas sales and refer to the sum paid by the holder of a concession to the Federation based on the volume of gas produced and sold from the fields within the concession in line with the following fiscal terms:¹⁰¹

 - onshore 7% of gas sale
 - offshore 5% of gas sale
- ❑ **Capital gains tax:** if a company disposes of a capital asset, capital gains accruing from the disposal are subject to tax under the Capital Gains Tax Act 2004 at the rate of 10%.

95 Ernst & Young, 2015 Global oil and gas tax guide.

96 Ibid.

97 Ernst & Young, "2015 Worldwide corporate tax guide - Nigeria," <[http://www.ey.com/Publication/vwLUAssets/Worldwide_corporate_tax_guide_2015/\\$FILE/Worldwide%20Corporate%20Tax%20Guide%202015.pdf](http://www.ey.com/Publication/vwLUAssets/Worldwide_corporate_tax_guide_2015/$FILE/Worldwide%20Corporate%20Tax%20Guide%202015.pdf)> (15 July 2015).

98 Ibid.

99 Ibid.

100 Ernst & Young, 2015 Worldwide corporate tax guide – Nigeria.

101 NEITI, Financial, physical and process audit: An independent report assessing and reconciling physical and financial flows within Nigeria's oil and gas industry 2012, 2015, <http://neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf> (20 May 2015).

- ❑ Education tax: amounts to 2% of the profits of a company. This tax is subtracted from the profits before petroleum profits tax is calculated.
- ❑ NDDC tax:¹⁰² Any oil producing or gas processing company in the Niger Delta area, on shore and offshore, is required to make an annual contribution of 3% of their total annual budget.¹⁰³
- ❑ Indirect taxes: parts imported for the production of oil and gas are exempt from import duties and VAT.
- ❑ Withholding tax (WHT): Under Nigerian law, certain income is subject to withholding tax (WHT) regulations. Income subject to WHT includes rent, interest, dividends, fees, commissions and payments in respect of contracts. Thus, if a company makes a payment on one of these types of income, the company is required by law to deduct WHT from the payment at the applicable rate, which is 10% for most transactions, and pay this sum to the tax authorities. However, WHT does not apply to dividends declared from profits that have incurred PPT. Nigeria has double taxation treaties with Belgium, Canada, China, France, the Netherlands, Pakistan, Philippines, Romania, South Africa and the United Kingdom. These countries are granted a reduced rate of WHT, usually at 75% of the generally applicable WHT rates. Thus, the applicable rate of WHT for treaty countries on interest, dividends and royalties is generally 7.5%.¹⁰⁴
- ❑ Pay As You Earn (PAYE) taxes: In addition to withholding taxes, companies in the oil and gas sector make deductions of tax from employees' remuneration – Pay As You Earn – and pay this to the states in which their operations are located.¹⁰⁵
- ❑ Since the Nigerian Oil and Gas Content Act was passed in 2010, every entity awarding a contract in the upstream sector of the Nigerian oil and gas industry should deduct and remit 1% to the National Content Development Fund. The 1% mandatory deduction is not applicable to contractual arrangements executed prior to 22 April 2010 even if ongoing after that date.¹⁰⁶
- ❑ Resource rent tax: oil companies pay rent for holding an oil prospecting licence (OPL) or an oil mining lease (OML). The rates depend on the type of licence, varying between NGN 200-500 (=US\$ 1-2.50) per square kilometre of oil producing area.
- ❑ There are several small taxes for oil companies, such as US\$ 0.12 per kilometer of pipeline per year, US\$ 0.02 of oil terminal dues per barrel of crude oil exported, and other small items.

102 The NDDC is a Federal government agency established in 2000 with the mandate to develop the oil-rich Niger Delta region of southern Nigeria, <<http://www.nddc.gov.ng/about%20us.html>> (15 July 2015).

103 NEITI Audit 2006-2008, 2011, <<http://www.neiti.org.ng/sites/default/files/documents/uploads/neiti-2006-2008-financial-report-fiinal-300112.pdf>> (15 July 2015).

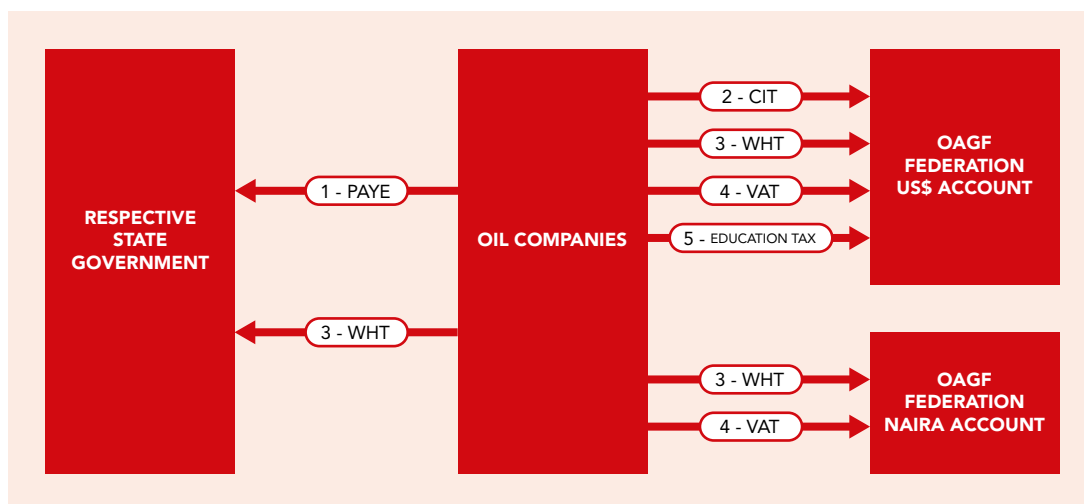
104 Ernst & Young, Global oil and gas tax guide 2015.

105 NEITI Audit 2006-2008, 2011.

106 US Energy Information Administration website, <<http://www.eia.gov/beta/international/analysis.cfm?iso=NGA>> (15 July 2015).

In Figure 2 the financial flows from oil and gas companies to the Government of Nigeria (both State and Federal level) is illustrated.

Figure 2: Financial flows for oil and gas sectors to the Government of Nigeria¹⁰⁷



Anti-tax avoidance legislation

Nigeria does not have any explicit rules against common tax avoidance methods such as thin capitalisation¹⁰⁸ or the practice of lending excessive amounts of money to subsidiaries so that all their income is siphoned out in the form of interest – but it does have general anti-tax avoidance rules. The transfer pricing regulation issued by Federal Inland Revenue Service (FIRS, the Nigerian tax authority), for example, became effective on 2 August 2012. Companies carrying on transactions with related parties are required to conduct transfer pricing studies to ensure that connected transactions have been appropriately priced to conform with arm’s length standards, thereby preventing companies from shifting profits as a result of transfer mispricing.¹⁰⁹

Tax holidays

Over the years the Nigerian government has adopted various and overlapping incentive schemes to attract both local and foreign investment. Tax exemptions, also known as tax holidays, are one of the most widespread tax incentives and are provided under the Industrial Development (Income Tax

107 NEITI audit 2006–2008, 2011, <<http://www.neiti.org.ng/sites/default/files/documents/uploads/neiti-2006-2008-financial-report-fiinal-300112.pdf>> (15 July 2015).

108 Thin capitalization occurs when companies are provided with an incentive to finance their operations with debt rather than equity, especially in high tax countries. This is possible when interest on debt is deductible from taxable income at the corporate level; Blouin et al., “Thin Capitalization Rules and Multinational Firm Capital Structure”, 2014, IMF Working Paper; <<http://www.imf.org/external/pubs/ft/wp/2014/wp1412.pdf>> (15 July 2015)

109 Ernst & Young, Global oil and gas tax guide 2015.

Relief) Act of 1971.¹¹⁰ Tax exemption simply means that taxes normally paid to the government are waived, either partially or completely, for a specified period of time. All limited liability companies registered in Nigeria may apply for pioneer status, which is granted to companies in industries that are considered vital to Nigeria's economic development.¹¹¹ The granting of pioneer status gives a company a preferential position in getting established, usually through a complete or partial exemption from income tax. Tax exemptions in Nigeria are normally given for a period of three years, with the possibility of extension for another two years. If the company is established in a disadvantaged rural area, the maximum exemption period is seven years.¹¹² There is no publicly available information identifying the number of companies benefiting from the Industrial Development (Income Tax Relief) Act. In the "list of pioneer industries and pioneering products" published on the website of the Nigerian Investment Promotion Commission, 71 industries are included, basically covering the whole economy (including "Mineral oil prospecting and production" and "Manufacture of gas and distribution").¹¹³

According to the Industrial Development (Income Tax Relief) Act, awarding of extensions to tax holidays depends on a number of criteria, including:

- ❑ the rate of expansion, standard of efficiency and the level of development of the company;
- ❑ the implementation of any scheme
 - for the utilization of local raw materials in the processes of the company; and
 - for the training and development of Nigerian personnel in the relevant industry;
- ❑ the relative importance of the industry in the economy of the country;
- ❑ the need for the extension, in relation to the location of the industry; and
- ❑ such other relevant matters as may be required.

In 2014, the Nigerian Investment Promotion Commission (NIPC) published Pioneer Status Incentive Regulations which provided specific provisions to the law and stipulated further conditions for the application of a pioneer status.¹¹⁴

Extended tax holidays

In the oil and gas industry in Nigeria, a 10-year tax holiday was given to the joint venture company Nigeria LNG under the 1990 Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Act.¹¹⁵ The details of this tax incentive law are covered in Chapter 4.

To date in Nigeria, no company other than Nigeria LNG has benefited from a 10-year tax holiday enacted by law. However, in May 2012, PwC reported that a bill to amend the Companies Income

110 Industrial Development (Income Tax Relief) Act of 1971, <http://www.placng.org/new/laws_of_nigeria3.php?sn=203> (15 July 2015).

111 Ernst & Young, Global oil and gas tax guide 2015.

112 Op. cit., Industrial Development (Income Tax Relief) Act of 1971.

113 Nigerian Investment Promotion Commission, undated, Investment Incentives, <<http://nipc.gov.ng/index.php/invest-in-nigeria/investment-incentives.html>> (15 July 2015).

114 Ernst & Young website, <<http://www.ey.com/GL/en/Services/Tax/International-Tax/Alert--Nigerian-Investment-Promotion-Commission-releases-Pioneer-Status-Incentive-Regulations>> (15 July 2015).

115 Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Act, <http://www.placng.org/new/laws_of_nigeria3.php?sn=347> (15 July 2015).

Tax Act 2004 was passed at the National Assembly (Senate).¹¹⁶ The proposed amendment aims to provide additional tax incentives for gas utilization, mining sectors and businesses located in areas with inadequate infrastructure.

According to PwC, the key changes include:¹¹⁷

1. An increase in the rate of rural investment allowance from 10% to 20% for companies that incur capital expenditure on un-tarred roads within 10kms (instead of the current 20kms) of their businesses.
2. The introduction of a new provision for a 10-year tax holiday to any company established in a place where no infrastructure such as electricity, water, or tarred road is provided by the government.
3. Increased tax-free period for mining companies from three to five years.
4. Increased tax free period for gas utilization companies (downstream operations) from five to seven years.

It could not be confirmed whether the bill was indeed passed, but it has been discussed in the Nigerian Senate and is available online.¹¹⁸ As explained during the debate in Senate, *"The broad philosophy behind the amendments sought through this Bill is to stimulate the growth of economic activities within the industry mining sector of the economy in order to create employment opportunities."* In relation to the increase in the tax-free period to 10 years being proposed for companies engaged in gas-related industries it is stated that the Bill *"will help in the development of gas consumption methods in this country that will lead to delivery of cooking gas through pipes to our homes."*¹¹⁹ In a comment on the bill by PwC, *"The proposed tax incentive should perhaps apply to all companies in Nigeria. The reason for this, which is not far-fetched, is that many companies do not rely on water or electricity provided by government. Also in many cases tarred roads are as poorly maintained as un-tarred ones. Consequently, this means virtually all companies operating in Nigeria (including those located in cities) should be eligible for the incentive."*¹²⁰

However, as was explained in Chapter 1.3, the tendency internationally has been to advise governments to abandon tax incentives, as their effectiveness is disputed and the losses they cause for developing countries are enormous. Following this line of reasoning, this bill is expected to lead to even fewer foreign companies paying their fair share of taxes in Nigeria, a country that already has a problem in ensuring sufficient domestic revenue mobilisation from the private sector and from ordinary

116 PwC website, <http://www.pwc.com/en_NG/ng/pdf/proposed-amendments-to-companie-income-tax-act-in-nigeria.pdf> (15 July 2015).

117 PwC website, <http://www.pwc.com/en_NG/ng/pdf/proposed-amendments-to-companie-income-tax-act-in-nigeria.pdf> (15 July 2015).

118 A Bill for an Act to Amend the Companies Income Tax Act Cap. C21 LFN 2004, <<http://www.nassnig.org/document/download/828>> (15 July 2015).

119 Nigerian Senate website, <<http://www.senate.gov.ng/nl/2012-09-27-14-06-02/lead-debates/373-a-bill-for-an-act-for-amendment-of-companies-income-tax>> (15 July 2015).

120 PwC website: <http://www.pwc.com/en_NG/ng/pdf/proposed-amendments-to-companie-income-tax-act-in-nigeria.pdf> (15 July 2015).

citizens alike.¹²¹ The country relies heavily on taxing of natural resources: the share of non-renewable natural resources in total fiscal revenue is 76% in Nigeria.¹²² And compared to other African countries with a relatively balanced mix of different types of taxes, such as Kenya and South-Africa, Nigeria relies almost entirely on one single type of tax.¹²³ As a consequence of this new bill, the only substantial source of taxation will be seriously eroded and other foreign companies will be allowed to benefit from tax breaks as significantly as the three oil companies in this case study.

Other changes to the legislative framework

The Nigerian Oil and Gas Content Act 2010 (commonly known as the NOGIC Act) was signed into law on 22 April 2010 and became effective from this date. The NOGIC Act is the legal framework and mechanism for creating an environment that increases local capacity building and it will be implemented by the Nigerian Content Monitoring Board. From 2010 on, every entity awarding a contract in the upstream sector of the Nigerian oil and gas industry should deduct and remit 1% to the National Content Development Fund.

The Petroleum Industry Bill (PIB), which was initially proposed to the National Assembly in 2008, is expected to change the organisational structure and fiscal terms governing the oil and natural gas sectors if it becomes law. IOCs are concerned that proposed changes to fiscal terms may make some projects commercially unviable, particularly deep-water projects that involve greater capital spending. Some of the most contentious areas of the PIB are the potential renegotiation of contracts with IOCs, changes in tax and royalty structures, and a mandatory contribution by IOCs of 10% of monthly net profits to the Petroleum Host Communities Fund.¹²⁴

The latest draft of the PIB was resubmitted to the National Assembly by the Ministry of Petroleum Resources in July 2012. Given the regulatory uncertainty there has not been a licensing round since 2007 and as a result, there has been less investment in new projects.

The regulatory uncertainty has also slowed the development of natural gas projects as the PIB is expected to introduce new fiscal terms to govern the natural gas sector too.¹²⁵

121 In Nigeria, a television soap opera “Binding Duty” was broadcast to remind citizens of their responsibility to pay taxes. With a weekly audience of 50 million, the programme has been very successful in raising awareness of the importance of taxation among ordinary citizens. OECD, 2014, *Fragile States 2014 – Domestic Revenue Mobilisation in Fragile States*, <<http://www.oecd.org/dac/governance-peace/conflictandfragility/docs/FSR-2014.pdf>> (15 July 2015).

122 Op. cit., OECD, 2014.

123 African Development Bank, 2010, *Domestic resource mobilization across Africa: trends, challenges and policy options*, <http://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/C-10%20Note%20%20English%20%28final%29_for%20posting%202.pdf> (15 July 2015).

124 US Energy Information Administration website, <<http://www.eia.gov/beta/international/analysis.cfm?iso=NGA>> (15 July 2015).

125 Ibid.

3.3 Financial and tax transparency

The Nigerian government has demonstrated a strong commitment to the Nigeria Extractive Industry Transparency Initiative (NEITI).¹²⁶ Nigeria's steps toward greater revenue transparency began in 2003 to 2004 with President Obasanjo's endorsement of the NEITI. The NEITI Act was officially signed into law in May 2007. The government's commitment to transparency is also demonstrated through the Fiscal Responsibility and Public Procurement Laws, as well as the Freedom of Information Act, which was signed into law in 2011.¹²⁷

The government measures onshore production at export terminals, while NEITI publishes 'physical and process' audit reports as well as financial audit reports, which are intended to audit companies' production data.¹²⁸ Thorough and sustained implementation of these policies and the determination to tackle other critical issues, including improved transparency of government budgets at the federal, state and local level, depends on the will of the current government. A major problem in Nigeria is that the government has limited capacity to verify how much oil and gas is being produced. The national petroleum company, NNPC, is not involved in production itself but instead has given concessions or licences (production sharing contracts) that are operated by international joint venture partners. This means that companies are responsible for declaring the produced volumes without any government verification. In addition there is the problem of oil theft or 'bunkering', which has robbed the Nigerian government of substantial revenues.¹²⁹ Finally, some major oil companies seemingly object to the publication of company-specific financial flows as demanded by NEITI.¹³⁰ A major problem is that NEITI reports do not provide a sufficient comparative basis concerning what companies reportedly pay and what the government reportedly receives.

In relation to the case of NLNG, it is unclear how or if the NNPC's income from NLNG finds its way to Nigerian government accounts, and there is no publicly available information on how this is accounted for. Auditors have raised this question in the Nigerian Extractive Industry Transparency Initiative (NEITI) reports. In the 2009-2011 NEITI report auditors commented that *"There is a need to confirm the ownership of the 49% investments in NLNG – Is it for the benefit of the Federation, or the Federal Government, or NNPC itself?"*¹³¹ In the recently published 2012 audit of the oil and gas sectors, NEITI commented: *"... , it is expected that the federation should at least benefit from the huge investments in NLNG through operational surplus of NNPC if indeed the investment in*

126 Natural Resource Governance Institute website, <<http://www.resourcegovernance.org/countries/africa/nigeria/overview>> (15 July 2015). For more info on NEITI see <<http://www.neiti.org.ng/>>.

127 Freedom of Information Coalition, 2011, <http://www.foicoalition.org/foi_bill/index.htm?35,7> (15 July 2015).

128 NEITI, 2012, Physical and Process Final Audit Report; <http://neiti.org.ng/sites/default/files/pdf_uploads/EITI-Physical-And-Process-Final-Audit-Report-2009-2011.pdf> (15 July 2015).

129 Financial Times, "Nigeria losing \$1bn a month to oil theft," 2012, <<http://www.ft.com/intl/cms/s/0/61fb070e-bf90-11e1-a476-00144feabdc0.html#axzz3g3SCokuz>> (15 July 2015).

130 Op. cit., Shaxson, 2009.

131 NEITI, 2012, Financial Audit: An Independent Report Assessing and Reconciling Financial Flows within Nigeria's Oil and Gas Industry – 2009 to 2011, p. 19, <http://neiti.org.ng/sites/default/files/pdf_uploads/NEITI-EITI-Core-Audit-Report-Oil-Gas-2009-2011-310113-New.pdf>.

*NLNG actually belongs to NNPC.*¹³² NNPC has not proved that financial flows from NLNG (dividends, loan and interest repayments) – which by end 2012 amounted to US\$ 11.6bn, have been remitted to the Federation accounts.¹³³

More generally, numerous media reports, government investigations and academic articles have reported that tax evasion and avoidance have been major problems over decades in the Nigerian oil and gas industry.¹³⁴

132 NEITI, 2015, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria's Oil and Gas Industry 2012, p.325, <http://www.neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf>.

133 NEITI, 2012, Financial Audit: An Independent Report Assessing and Reconciling Financial Flows within Nigeria's Oil and Gas Industry – 2009 to 2011, p. 325 NEITI, 2014, Nigeria Annual Activity Report 2013, p. 16 <<http://www.neiti.org.ng/sites/default/files/news/uploads/eiti-neiti-activity-report-2013-final.pdf>> and NEITI, 2015, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria's Oil and Gas Industry 2012, p.325, <http://www.neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf>.

134 For an overview of major cases of tax avoidance in Nigeria, please refer to O.J. Otusanya, "The role of multinational companies in tax evasion and tax avoidance: The case of Nigeria," 2011, <<http://www.sciencedirect.com/science/article/pii/S1045235410001802>> (15 July 2015).

4 The case of Nigeria Liquefied Natural Gas Company

This chapter describes the case of Nigeria Liquefied Natural Gas Company (NLNG), Nigeria's largest gas production facility, with a focus on an extended tax holiday awarded to NLNG in 1990 and which has benefited three foreign oil companies for a period of 12 years. It gives an introduction to the joint venture company NLNG (section 4.1), followed by an explanation of the extended tax holiday provided to NLNG in Nigeria (section 4.2). An analysis is made of the tax potentially lost to the Nigerian government and to its people due to this tax holiday – specifying the share attributable to Shell, Total and Eni (section 4.3).

4.1 Introduction to Nigeria Liquefied Natural Gas Company (NLNG)



The creation of NLNG

From the late 1960s, the Nigerian government and several oil companies, including Shell and BP, negotiated for a Nigerian LNG (liquefied natural gas) scheme that would be based on Bonny Island in Rivers State in the Niger Delta. In 1981 US based Phillips Petroleum Company, the technical leader, withdrew, and when UK based BP also withdrew, the scheme stopped. Shell decided to take the technical lead and continue with the project given that it offered possibilities to process associated gas and reduce gas flaring.¹³⁵ In 2014, the Managing Director of NLNG stated that *“part of the mission for the establishment of NLNG was to ensure that gas, which was hitherto flared, was converted into economic benefits for the country. NLNG has converted over 4,000 trillion cubic feet of gas since its inception in 1999”*.¹³⁶

The joint venture operation Nigeria LNG Company (NLNG) was formally incorporated in 1989. After long negotiations with the Nigerian government it was announced in November 1995 that a final investment decision had been made regarding NLNG, in which shareholders decided to build a liquefied natural gas plant in Finima, Bonny Island, Rivers State, Nigeria (see Figure 3).¹³⁷ A consortium of engineering firms including Technip, Snamprogetti, M.V. Kellogg and Japan Gas

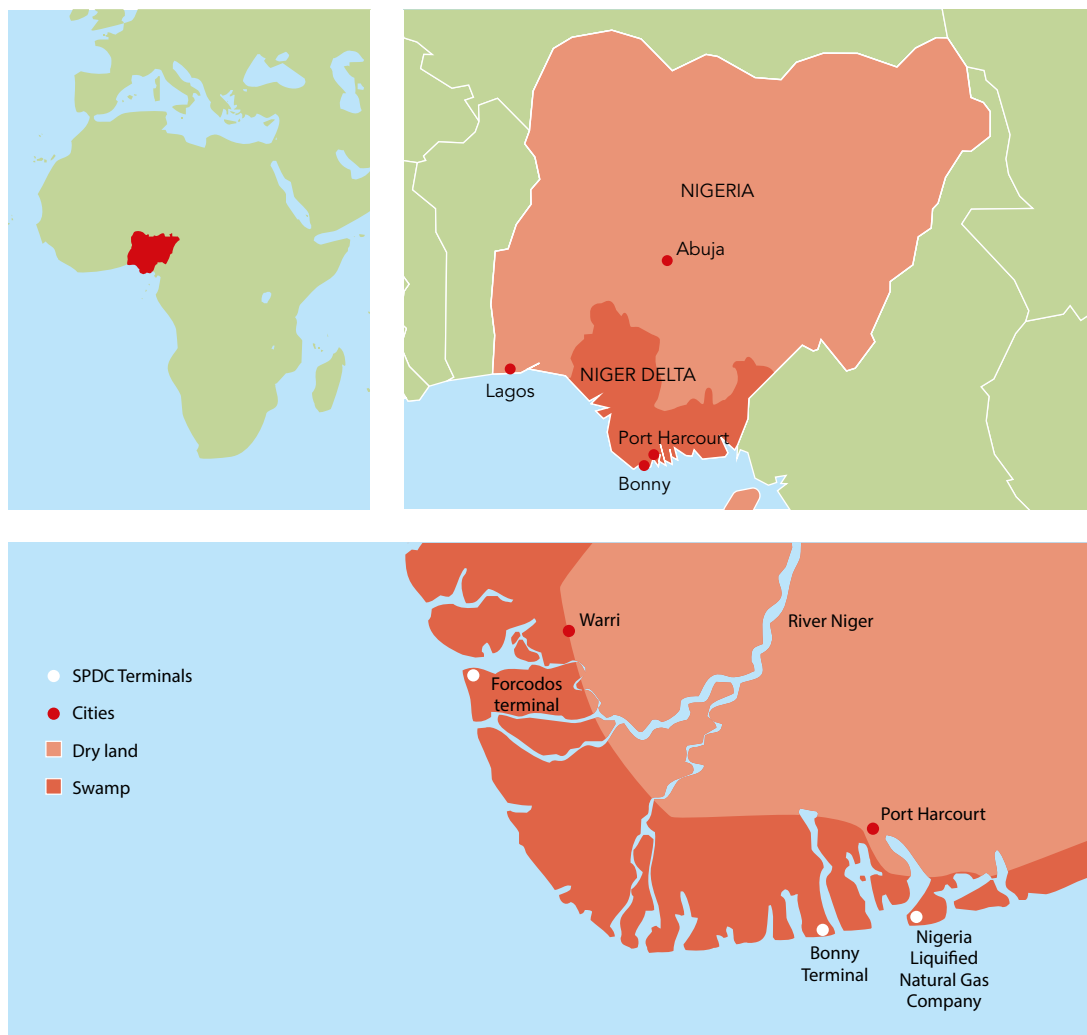
135 Op. cit., K. Sluyterman, 2007, p.343–349.

136 New Telegraph, “Gas flaring: NLNG adapts 4,000 trn scuf of gas,” 2014, <<http://newtelegraphonline.com/gas-flaring-nlng-adapts-4000-trn-scuf-gas/>> (15 July 2015).

137 Nigeria LNG website, <<http://www.nlng.com/>>.

Corporation (TSKJ) started construction of the LNG plant in 1996. They finished construction in August 1999, and operations started in September 1999.¹³⁸

Figure 3 Location of NLNG Plant at Bonny Island, Nigeria¹³⁹



138 Nigeria LNG, 2015, Facts and figures on NLNG 2015, <http://www.nlng.com/Media-Center/Publications/Facts_and_figures_2015.pdf> (15 July 2015).

139 Sources: <http://news.bbc.co.uk/2/hi/uk_news/7510645.stm>; <http://pipelinesinternational.com/news/nigerian_oil_pipeline_on_target/043518/>.

Box 3: What is LNG?

Liquefied natural gas (LNG) is gas that has been cooled to about -162°C (-260°F) for shipment and/or storage as a liquid. The liquid volume is about 600 times smaller than the gaseous volume. In this condensed form, natural gas can be shipped in special tankers to terminals in other countries. At these terminals, the LNG is returned to its gaseous form and transported by pipeline to distribution companies, industrial consumers and power plants. Liquefying natural gas provides a means of moving it long distances where pipeline transport is not feasible, meaning that regions with vast reserves, but which are too distant from end-use markets to be connected by pipeline, such as in Nigeria, can gain access to those markets more easily.¹

1 US Energy Information Administration "What is LNG?," 2014, <http://www.eia.gov/energyexplained/index.cfm?page=natural_gas_lng> (1 April 2015).

Description of NLNG

According to its website, NLNG was set up to harness Nigeria's vast natural gas resources and produce LNG and natural gas liquids (NGLs) for export. It extracts natural gas from the ground, purifies it and liquefies it to LNG so that it can be transported through pipelines or LNG carriers to customers. The NLNG plant currently utilises both non-associated gas and oil-associated gas which was formerly wasted through flaring. NLNG operates six LNG trains¹⁴⁰ with a total capacity of 22 million tons per annum (mtpa).¹⁴¹ Plans for building a seventh train that will lift the total production capacity to over 30 mtpa LNG are currently at an advanced stage. The main destination of the Nigerian gas is Europe (80–90% of total production).¹⁴² NLNG currently has LNG sales purchase agreements (SPAs) with 11 buyers, including Enel, Gas Natural, Botas, GDF Suez, GALP Gas Natural, BG LNG, Endesa, ENI, Iberdrola, Shell International Trading Middle East Ltd and Total Gas and Power Ltd.¹⁴³ NLNG accounts for approximately 7% of the world's total LNG supply.¹⁴⁴

NLNG's mission is *"to market, produce and deliver liquefied natural gas and natural gas liquids to buyers safely, reliably and profitably, growing our company and its people to their full potential, and being a trusted partner with all our stakeholders in the sustainable development of Nigeria's gas industry and of NLNG's host communities"*.¹⁴⁵

140 An LNG train is a liquefied natural gas plant's liquefaction and purification facility, <http://en.wikipedia.org/wiki/LNG_train>.

141 Nigeria LNG, 2015, Facts and Figures on NLNG 2015.

142 Annual Accounts NLNG 2009, p.12.

143 Op. cit., Nigeria LNG, 2015.

144 Shell Nigeria website, <<http://www.shell.com.ng/aboutshell/our-business/bus-nigeria/lng.html>> (15 July 2015).

145 Nigeria LNG website, <<http://www.nlng.com/Our-Company/Pages/Our-Mission,-Our-Vision.aspx>> (15 July 2015).

The company's vision is described as follows: "Our vision: a global LNG company helping to build a better Nigeria.

- ❑ *Nigeria LNG will be a global LNG company renowned for its operational excellence, cost leadership, high Health, Safety and Environmental (HSE) standards and for honesty and integrity. We will be helping to build a better Nigeria by utilising the country's gas resources and helping to put out the flares, thus diversifying the economy and cleaning up the environment.*
- ❑ *We will set the standards in community relations and technology transfer to Nigerians and actively promote the sustainable development of Nigerian businesses. We will provide to our shareholders a good return on their investment.*
- ❑ *We will provide for our staff an exciting and fulfilling place to work and the opportunity to develop their potential. We will execute and operate our business in Nigeria with an international outlook and mindset."*

Ownership structure

The company is jointly owned by Nigerian National Petroleum Corporation (49%), Shell Gas B.V. (25.6%), Total LNG Nigeria Ltd (15%) and Eni International N.A. (10.4%). The consortium of European oil companies holds the majority stake – 51% – of the joint venture. Shell is the biggest shareholder of the three foreign oil companies, as well as NLNG technical advisor. The company has two wholly owned subsidiaries: Bonny Gas Transport (BGT) Limited and NLNG Ship Management Limited (NSML). Bonny Gas Transport Limited was established in 1989, following the incorporation of Nigeria LNG Limited, to provide shipping capacity for NLNG and is incorporated in Bermuda.¹⁴⁶

Figure 4 outlines the corporate structure of NLNG, including the ownership structure of the three foreign shareholders, Shell, Total and Eni.

Key financial data

The key financial data of Nigeria LNG are provided in Figure 3 and Table 2 below. Since it started operating in 1999, its turnover has steadily increased (thanks to an increased production capacity) from US\$ 2.3 billion in 2004 to US\$ 9.7 billion in 2013 (with an even higher peak of US\$ 11.6 billion in 2012). Between 2004 and 2013, the company has realised a total profit after tax of at least US\$ 29.5 billion.¹⁴⁷ According to NLNG's Chief Executive Officer, the company's profits have been even higher, totaling US\$ 80 billion since inception, US\$30 billion of which was in the last three years.¹⁴⁸ These last figures could not be confirmed elsewhere so should be used with caution.

In terms of taxes paid it should be noted that between 1999 and 2009, NLNG made no tax payments to the Nigerian government due to the 10-year tax holiday decreed by the Nigeria LNG Act (see section 4.2 below). In the subsequent two years (2010 and 2011), income tax was still not paid as a result of carrying forward deferred tax assets from the previous 10 years. For reference purposes, the main figures from NLNG's annual accounts will be made available through SOMO's website..

¹⁴⁶ Nigeria LNG, Facts and figures on NLNG, 2015, p.7.

¹⁴⁷ Annual Accounts NLNG, 2008-2013. This is a conservative estimate as the financial data for the period 1999–2003 were not obtained.

¹⁴⁸ B. Omotowa, "Nigeria: In need of dreamers, of a certain kind," 2014, <<http://www.slideshare.net/NigeriaLNG/babs-omotowa-havard-university-speech>> (15 July 2015).

Figure 5: NLNG turnover, profit after tax, and total tax paid

2004-2013, in million US\$

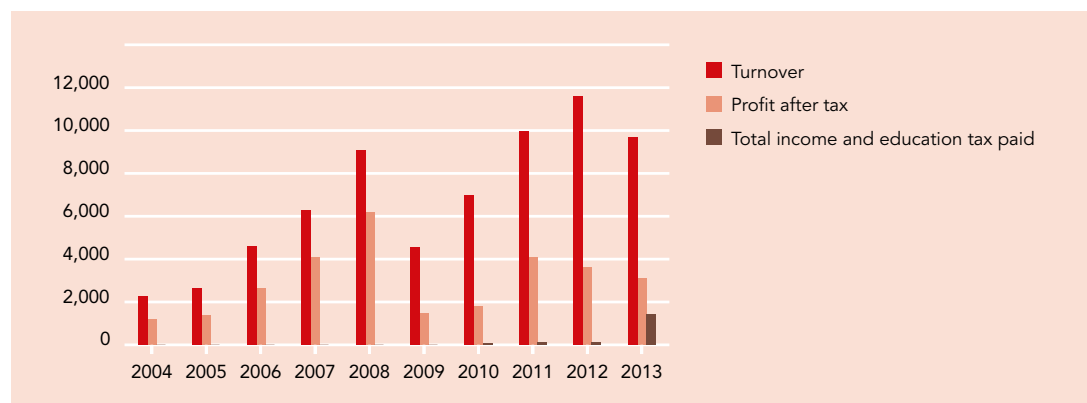


Table 2: Key financial data of Nigeria LNG, 2004-2013¹⁴⁹

All amounts in million US\$

Financial key data NLNG	Total 2004-2013	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
Turnover	67,619	9,668	11,592	9,962	6,968	4,542	9,067	6,286	4,602	2,648	2,284
Profit before tax	31,787	4,285	5,321	4,719	2,648	1,033	5,659	3,590	2,335	1,193	1,004
Deferred tax assets [1]				-718	-935	241	326	292	310	198	173
Deferred tax liabilities [1]		13	1,597								
Income tax charge		1,321	1,597	717	935	62					
Education tax charge		102	119	107	65	0					
Income from subsidiary company [2]		225	0	166	150	280	183	214	0	0	0
Profit after tax	29,520	3,087	3,605	4,061	1,798	1,492	6,168	4,096	2,645	1,391	1,177
Total income and education tax actually payable [3]	1,700	1,410	119	106	65	0	0	0	0	0	0
Effective tax rate [4]	5.3%	33%	2%	2%	2%	0%	0%	0%	0%	0%	0%

149 Source: NLNG Annual Accounts, 2008–2013.

Notes to Table 2:

- [1] *Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Deferred tax assets are calculated at the tax rates that are expected to apply in the period when the asset is realised. Deferred tax is charged or credited to income statements, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity (source: NLNG Annual Accounts 2013, p.11).*
- [2] *Income from subsidiary companies relates to dividend income received from the 2 wholly-owned subsidiaries of NLNG, Bonny Gas Transport Ltd. and NLNG Ship Manning Ltd.*
- [3] *Between 1999 and 2009, no income tax is paid because of the tax relief period of 10 years as established in the Nigeria LNG Act; In 2010 and 2011, no income tax is payable because it is deducted from deferred tax assets built up during the 10-year tax holiday; In 2012, no income tax is payable because of the build-up of deferred tax liabilities*
- [4] *Calculated as 'total income and education tax paid' divided by 'profit before tax'. It should be noted that for the year 2012, the tax paid by NLNG is lower than the tax reported in the income statement, as a large share of the income tax is booked as deferred tax liability. The basis for the effective tax rate is therefore the total tax minus the deferred tax liability.*

Contribution to the national and local economy

NLNG claims to be making a significant contribution to the national and local economy. According to NLNG's website, "the Nigeria LNG project is considered one of the most important economic projects being carried out in Nigeria" and its contribution to the Nigerian economy includes:¹⁵⁰

- ❑ environmental hazard reduction through reduced gas flaring;
- ❑ paying dividends of almost US\$ 30 billion, out of which 49% went to the Federal Government of Nigeria;
- ❑ generating foreign direct investment – over US\$ 14 billion worth of assets was financed mainly by NLNG's stakeholders;
- ❑ contributing about 1% to Nigeria's GDP;
- ❑ creating more than 2,000 jobs each construction year; overall, the major sub-contractors employed about 18,000 Nigerians in technical jobs in the base project;
- ❑ supporting the development of community and Nigerian contractors to enable them achieve standards of excellence;
- ❑ community development – host communities and the local economy enjoyed a boom as a result of capital inflow during NLNG's construction phase; in addition, over Naira 25 billion (around US\$ 125 million) has been spent by the company on community projects over the years.

There is very little public information on NLNG's tax payments. In the company's NLNG Facts & Figures report 2015 it states that "as a good corporate citizen, NLNG contributes to national wealth and economic wellbeing of states in which it operates, by paying all applicable taxes and tariffs. In 2014, the company's corporate income tax amounted to about N220 billion (around US\$ 1 billion),

150 Nigeria LNG, Facts and figures on NLNG, 2015.

thus making NLNG by far the highest tax payer in Nigeria and Sub-Sahara Africa".¹⁵¹ On the company's website it was stated that "NLNG is to pay over US\$1 billion as Company Income Tax (CIT) to the federal government in 2014."¹⁵²

How these taxes are benefiting the Nigerian government could not be verified as the NEITI audits for these years are not yet available. But based on past experience these data cannot be taken at face value. As explained in more detail below, NEITI audits have shown that there is a lack of clear reporting of payments to the government. More importantly, the company is completely ignoring the fact that it has not paid any income tax for a period of 12 years, as explained in detail in section 4.2 and 4.3.

- ❑ NLNG has not paid any royalties on its gas sales. This was confirmed by Eni, who wrote in response to the draft findings that NLNG is not subject to the payment of royalties since:
 - royalty is due and payable on the gas extracted by producers from wells and sold to buyers; and
 - NLNG does not extract gas from wells but process the gas received from the Producers into LNG and other by products which are not subject to royalty.
- ❑ Total wrote that "in Nigeria as in any other countries, royalty on gas is due by the producer of gas and not by the company buying gas and liquefying it into LNG. As such, NLNG is not liable to royalty. Royalty on the gas purchased by NLNG is payable by the producer of such gas. There is no royalty on sales of LNG." This is in line with the latest NEITI audit, which states that royalties on gas sales refer to the sum paid by the holder of a concession to the federation based on the volume of gas produced and sold from the fields within the concession in line with the following fiscal terms:¹⁵³
 - onshore 7% of gas sale
 - offshore 5% of gas sale

Dividend distribution

The NLNG dividend is paid to shareholders, which means that 49% of the dividend is paid directly to the government-owned NNPC. The latest NEITI audit explains that "the benefit flows (of NLNG as a whole) for the Federation are dividends and loan interest paid by NLNG to the government through NNPC". The total of dividends and loan repayments amount to US\$ 4.8 billion for the three-year period 2009 to 2011.¹⁵⁴ For the period 2006 to 2008, dividends amounted to US\$ 4 billion.¹⁵⁵ It is nevertheless unclear how or if the NNPC's income from NLNG finds its way to Nigerian government

151 Nigeria LNG, facts and figures on NLNG, 2015, p.29.

152 NLNG News, 2013, NLNG to Pay US\$1bn as company tax in 2014, <<http://www.nlng.com/News.aspx?id=109>> (1 April 2015).

153 NEITI, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria's Oil and Gas Industry 2012, 2015, <http://neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf> (15 July 2015).

154 In the NEITI audit report, only an aggregated amount is provided for dividend and loan repayments, so it is not clear how much of this relates to dividends only. NEITI, Financial Audit: An independent report assessing and reconciling financial flows within Nigeria's oil and gas industry – 2009 to 2011, p.89, 2012, <http://neiti.org.ng/sites/default/files/pdf_uploads/NEITI-EITI-Core-Audit-Report-Oil-Gas-2009-2011-310113-New.pdf> (15 July 2015).

155 NEITI, 2012, p.19.

accounts, and there is no publicly available information on how this is accounted for. Auditors have raised this question in the Nigerian Extractive Industry Transparency Initiative (NEITI) reports.

In the 2009-2011 NEITI report auditors commented that *“There is a need to confirm the ownership of the 49% investments in NLNG – Is it for the benefit of the Federation, or the Federal Government, or NNPC itself?”*¹⁵⁶ In the recently published 2012 audit of the oil and gas sectors, NEITI commented: *“... , it is expected that the federation should at least benefit from the huge investments in NLNG through operational surplus of NNPC if indeed the investment in NLNG actually belongs to NNPC.”*¹⁵⁷ It further states that NNPC is listed as not complying with the Fiscal Responsibility act regarding payments of its operating surplus to the Consolidated Revenue Fund (CRF).¹⁵⁸ NNPC however claims that it *“has Presidential approval to sequester the NLNG Dividend to fund all Gas related projects”*, and that it is unconstitutional to treat the dividends from NLNG as revenue that must be transferred to the Federal Account.¹⁵⁹ NNPC has not proved that financial flows from NLNG (dividends, loan and interest repayments) – which by end 2012 amounted to US\$ 11.6bn, have been remitted to the Federation accounts.¹⁶⁰ The NEITI Audit of 2012 furthermore states that *“the issue of the NLNG dividend has been the subject of previous audits and is being dealt with by the Inter-Ministerial Task Team (IMTT) set up by government to address remedial issues arising from NEITI audits. The position of NNPC remains that the Corporation has 49% equity in NLNG and has Presidential approval to sequester the NLNG Dividend to fund all Gas related projects.”*¹⁶¹

When assessing the generosity of this tax incentive, it should also be noted that Nigeria is heavily reliant on royalties from its natural resource extraction. However, unlike oil and mining contracts, companies operating in the gas sector in Nigeria are not subject to royalties.¹⁶² This may be changing. According to the latest Nigerian EITI audit that was published in 2015, companies need to pay

156 NEITI, 2012, Financial Audit: An Independent Report Assessing and Reconciling Financial Flows within Nigeria’s Oil and Gas Industry – 2009 to 2011, p. 19, <http://neiti.org.ng/sites/default/files/pdf_uploads/NEITI-EITI-Core-Audit-Report-Oil-Gas-2009-2011-310113-New.pdf >.

157 NEITI, 2015, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria’s Oil and Gas Industry 2012, p.325, <http://www.neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf >.

158 According to the Nigerian Constitution, all revenues raised or received by the State shall be paid into the Consolidated Revenue Fund of the State; <<http://nigerian-constitution.com/chapter-5-part-2-section-120-establishment-of-consolidated-revenue-fund/> >.

159 NEITI, 2015, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria’s Oil and Gas Industry 2012, p.325, <http://www.neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf >.

160 NEITI, 2012, Financial Audit: An Independent Report Assessing and Reconciling Financial Flows within Nigeria’s Oil and Gas Industry – 2009 to 2011, p. 325 NEITI, 2014, Nigeria Annual Activity Report 2013, p. 16 <<http://www.neiti.org.ng/sites/default/files/news/uploads/eiti-neiti-activity-report-2013-final.pdf> > and NEITI, 2015, Financial, Physical and Process Audit: An Independent Report Assessing and Reconciling Physical and Financial Flows within Nigeria’s Oil and Gas Industry 2012, p.325, <http://www.neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf >

161 NEITI, 2015, Financial, Physical and Process Audit: an independent report assessing and reconciling physical and financial flows within Nigeria’s oil and gas industry 2012, <http://neiti.org.ng/sites/default/files/pdf_uploads/2012-OIL-GAS-REPORT/2012-Oil-Gas-Audit-Report.pdf> (15 July 2015).

162 KPMG Professional Services, 2014, Nigeria’s Oil and Gas Industry Brief, p.13; <<https://www.kpmg.com/NG/en/IssuesAndInsights/ArticlesPublications/Pages/NigerianOilandGasBrief.aspx>>.

royalties on gas sales, based on the volume of gas produced and sold from the fields within the concession. The rates applicable are 7% for onshore gas production and 5% for offshore gas production. However, there is no information on any royalty payments by NLNG. Up until 2013, NLNG had in any case not contributed royalties to the Nigerian state. The uncertainty regarding revenue from royalty payments increases the importance of corporate income tax and other taxes levied on the gas sector.

Financiers of NLNG

A large number of financiers have been involved in financing NLNG. The base project (Trains 1 and 2), which cost US\$ 3.6 billion, was financed by NLNG's shareholders, NNPC, Shell, Total and Eni. For the expansion projects (Trains 3–6) that followed, the following financial institutions were involved in addition to the shareholding companies:¹⁶³

- ❑ for the LNG trains: African Development Bank, a group of 19 international banks led by BNP Paribas, Citigroup, Credit Lyonnais, MCC and West LB;
- ❑ for the LNG ships: Citibank, Credit-Suisse First Boston, ABN AMRO Bank, Credit Lyonnais, Fortis, ING Bank, HVB, Verein und Westbank, West LB, Standard Chartered Bank.

As additional shipping capacity has become necessary, Bonny Gas Transport has completed plans to acquire six new vessels which are currently being built and will be completed by 2016. Financing for the six vessels has been arranged with two international commercial banks as lenders: the Korean Finance Corporation and Korean Export-Import Bank (KEXIM).

4.2 The NLNG Act: an excessively generous 10-year tax holiday

As explained in section 3.2, the Nigerian government has, over time, put in place many different tax incentives to attract both local and foreign investment. In Nigeria, tax exemptions are provided under the Industrial Development (Income Tax Relief) Act of 1971 and are normally given for a period of three years, with the possibility of extension for another two years (totaling 5 years).¹⁶⁴ In the oil and gas industry in Nigeria, as an exceptional case, a 10-year tax holiday was given to NLNG, Nigeria's largest gas production facility, under the 1990 NLNG Act.¹⁶⁵

Comparing the NLNG Act with the regular Income Tax Relief Act

Table 3 outlines the provisions of the NLNG Act and how they compare to those for companies with ordinary pioneer status in Nigeria. The relevant laws are:

- ❑ for all companies: Industrial Development (Income Tax Relief) Act 1971;¹⁶⁶
- ❑ for NLNG only: Nigeria LNG (Fiscal Incentives, Guarantees And Assurances) Act 1990.¹⁶⁷

163 Nigeria LNG, Facts and figures on NLNG, 2015, p.57–59.

164 See <http://www.placng.org/new/laws_of_nigeria3.php?sn=203>.

165 See <http://www.placng.org/new/laws_of_nigeria3.php?sn=347>.

166 For full text of the Industrial Development (Income Tax Relief) Act 1971, see: <http://www.placng.org/new/laws_of_nigeria3.php?sn=203>.

167 For full text of the Nigeria LNG (Fiscal Incentives, Guarantees And Assurances) Act 1990, see: <http://www.placng.org/new/laws_of_nigeria3.php?sn=347>.

Table 3: Provisions of the NLNG Act compared to companies with ordinary pioneer status in Nigeria¹⁶⁸

Provisions under the Industrial Development (Income Tax Relief) Act 1971	Section	Provisions under the Nigeria LNG (Fiscal Incentives, Guarantees And Assurances) Act 1990	Section
CIT (corporate income tax) exemption for 3 to 5 years	10.1	CIT (corporate income tax) exemption for 10 years	2
Capital allowances carried forward	10.2 14.2	Capital allowances carried forward	8
	14.2	Interest on loans deductible	5.1 5.2
		No tax on cross-border interest payments by NLNG	6.1
No tax on dividends paid by the company	17.1 17.2 17.3	No tax on dividends paid by NLNG	6.2
		No tax on payments by NLNG for services provided by non-Nigerian companies or individuals	6.5
		No capital gains tax on transfer of shares in company or any other company connected to it	6.6
		No tax on profits of shipping companies owned by NLNG	6.8
		Exemption from withholding tax on shipping companies	6.9
		Exemption from all shipping regulations for shipping companies owned by NLNG	6.10
		Exemption from customs duties (import duties, taxes and all other duties, levies and charges) for NLNG or its contractors	7.1
		No export duties, taxes or other duties, levies or charges on the export of LNG or other hydrocarbons	7.7
		No restriction on set off of capital allowance accumulated during the tax relief period against assessable profits in the period following the end of the relief period	8

168 Industrial Development (Income Tax Relief) Act 1971 and Nigeria LNG (Fiscal Incentives, Guarantees And Assurances) Act 1990.

How NLNG benefited from the extended tax break

NLNG commenced production in 1999 after completion of the gas production facility at Bonny Island. According to the NLNG Act, NLNG enjoyed exemption on all taxes for its first 10 years of production, (October 1999 to October 2009). As can be seen in Table 3, the tax exemption also applied to the profits of shipping companies owned by NLNG, including NLNG shipping subsidiary, Bonny Gas Transport Ltd. This 100% subsidiary of NLNG was incorporated in Bermuda in 1989.¹⁶⁹

Apart from paying zero taxes for the first 10 years of production, the company was also allowed to build up a large reservoir of 'deferred tax assets' for future purposes. The NLNG Act states that the company is permitted to deduct interest paid during the tax relief period from taxable income, after the company's tax relief period ends, and to take capital allowance deductions after its tax relief period for property, plant and equipment purchased during the tax relief period, or over 10 years. At the end of the tax relief period, in October 2009, this deferred tax asset amounted to US\$ 2.1 billion.¹⁷⁰

Table 4 shows the accrual process from 2004 onwards, with 'Income tax (charged to the statement of profit and loss)' showing the tax as it appears in the yearly Income Statement, and the 'Income tax actually paid or payable' showing the actual cash tax payments (from the cash flow statement). In the row 'Income tax (charged to the statement of profit and loss)', positive numbers indicate that deductible costs were accumulated as discount on future tax payments. Negative numbers indicate that taxes were due, but in the two years following the tax holiday, taxes were not actually paid (as can be seen in the row 'Income tax actually paid or payable'. For reference purposes, the main figures from NLNG's annual accounts will be made available through SOMO's website.

As NLNG exploits liquefied natural gas in Nigeria – a commodity specifically excluded from the definition of 'petroleum' and therefore likely also to be excluded from the definition of 'petroleum operations' – a rate of 30% is applicable instead of the 85% tax rate for oil companies (with a reduced rate of 65.75% for the first 5 years).

¹⁶⁹ Nigeria LNG, Facts and figures on NLNG, 2015.

¹⁷⁰ NLNG Annual Accounts 2009, p.17, note 15b.

Table 4: Profit, income tax and deferred taxes of NLNG, 2004-2013¹⁷¹

Year	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
Profit before tax	4285	5321	4719	2649	1033	5659	3590	2335	1193	1004
Income Tax (charged to the statement of profit and loss)	-1436	-1592	-718	-935	179	326	292	310	198	173
Income tax actually paid or payable	-1321	0	0	0	0	0	0	0	0	0
Total deferred tax assets accrued	0	0	442	1160	2095	1916	1590	1298	988	790

All figures are in millions of US dollars.

For the years after the tax holiday expired, this means the following:

- ❑ The 2010 NLNG Annual Account reports that the firm was obliged to pay taxes amounting to exactly US\$ 1 billion.¹⁷² Of this total, US\$ 935 million was income tax, which was deducted from the US\$ 2.1 billion deferred tax asset built up during the 10 year tax holiday. The remaining US\$ 65 million was education tax, which was actually paid to the government.¹⁷³
- ❑ The 2011 NLNG Annual Report states that the firm was obliged to pay taxes amounting to US\$ 825 million. Of this total, US\$ 718 million was income tax, which was deducted from the deferred tax asset that NLNG had built up during the 10 year tax holiday, of which there was US\$ 1.16 billion left after US\$ 935 million was deducted in 2010. The remaining amount, US\$ 107 million was education tax, which was actually paid to the government.¹⁷⁴
- ❑ The 2012 NLNG Annual Report states that the firm was obliged to pay taxes amounting to US\$ 1.7 billion. Of this total, US\$ 118 million was education tax, while the remainder, US\$ 1.6 billion, was set aside as deferred tax liability. The company reported that no income tax is payable by the company due to unrelieved tax losses and unused capital allowances carried forward from prior years. However, as can be seen in Table 4, only US\$ 442 million was left as deferred tax assets. To delay the company from paying taxes, a 'deferred tax liability' of US\$ 1.15 billion is recorded under 'non-current liabilities' on the balance sheet. This means that in future the company will pay more company income tax based on a transaction that took place in 2012. According to information provided by Eni (see Annex 4), the deferred tax asset of US\$ 1.15 bn arose as a movement between tax relief enjoyed as a result of capital allowances brought forward from the pioneer/tax holiday periods and the accounting depreciation. The US\$1.15bn in 2012 is a deferred tax asset which represents the timing difference of tax impact between capital allowances and accounting depreciation of the qualified capital expenditures.

¹⁷¹ LNG Annual Reports Limited, 2008–2013.

¹⁷² No matter how improbable it sounds, according to the 2011 Annual Accounts this was exactly US\$ 1,000 million or 1 billion.

¹⁷³ NLNG Annual Accounts 2010, p.11.

¹⁷⁴ NLNG Annual Accounts 2011, p.20.

- The 2013 NLNG Annual Report states that the firm was obliged to pay taxes for an amount of US\$ 1.4 billion. Out of this total, US\$ 1.3 billion was payable as corporate income tax, and US\$ 102 million consisted of education tax. It is reported that with effect from 2013, the company is now liable to income tax payment for the first time. At the end of 2013, a total amount of US\$ 1.4 million is booked under the 'current tax liabilities' in the balance sheet. This is common practice and it is normally expected that after the year has ended and the tax return is filed, this amount becomes payable. In fact, in its response to the draft findings, Eni confirmed that "NLNG Company's income tax liability first crystalized in 2013 was paid in line with the law in 2014. Subsequently Company income tax liability has been promptly settled as and when due." (see Annex 4)

Figure 6: Interview with Nigerian tax authorities on tax holiday for Nigeria LNG

July, 2012 Vol 2.
FIRS News Bulletin


"NLNG Has Enjoyed 10 Years Abnormal Tax Holiday"- D/Oil & Gas

By Babarinde Ola Joe

It is common knowledge that the Nigeria LNG limited has been at the fore front of gas exploration in Nigeria, and the company has enjoyed an abnormal period of tax holiday for about ten years. This was disclosed by the Director, Oil and Gas, Mr Bamidele Ajayi in a recent interview with the Gauge Magazine crew.

While giving reasons for the pioneer status enjoyed by NLNG which expired in 2009, Mr Bamidele stated that it was government's initiative to encourage the liquefied gas industry at inception. "The reasoning then was that government thought Nigeria had more potentials in gas than crude, so the thought then was that they needed to develop it, and in doing so, they were given a tax holiday of 10 years, which is abnormal," he said. He however explained that upon the expiration of the tax holiday in 2009, it has been difficult to get them to clear up tax liabilities because of the complex clauses in the tax holiday document which made it an opened-ended document.

The D/Oil & Gas also explained the recent restructuring in the large tax which gave room to the creation of Oil and Gas as a department. According to him "going down memory lane from 1992 till date, there have been different changes to the



D/Oil & Gas, Bamidele Ajayi sharing his views on the oil and gas sector with Nneka Ifekwuna and Umar Yussuf

administration of the sector with the last being the merging with non-oil. But now, Management thought we should have the oil and non-oil separate. Even in the oil, we have the upstream which is the exploration, there is also downstream which deals with the marketing part and the servicing which is those providing services to the oil companies". While giving explanation on the modus operandi in the oil and gas, Mr Bamidele said not a few have misconceive the activities of the sector, which explains the misunderstanding of its activities. He regarded the activities of the sector as complex, highly regulated and most complex.

While answering a question on collection of taxes on royalties, Mr Bamidele stressed that over time he had explained that FIRS is not

mandated to collect taxes on royalties. According to him " royalties are paid to government and FIRS collects royalties for government, are they now saying we should be charging tax on what we have collected for government?" He spoke further, " you cannot charge tax on money paid to government because it is like asking us to charge tax on PPT.

The Petroleum Industry Bill (PIB) is one of the contentious issues in the society, and the D/Oil & Gas shared his views on this. He noted that it was unfortunate that FIRS was not part of the committee for the draft initially until the former EC FIRS compelled the Presidency to include FIRS in the sub-committee. Recalling his experience, Mr Bamidele noted that "our contribution was only technical because we were not in the main committee; "so far with what is in the public now, we noticed a few changes to our contributions. We have called their attention to it, which they noted were errors that will be corrected. We hope they are indeed errors", he quipped as the interview concludes.

source: FIRS, "NLNG Has Enjoyed 10 years abnormal tax holiday" – D/Oil & Gas, 2012, <<http://www.firs.gov.ng/Resource-Centre/Documents/Newsletter%20July%202012%20Vol.%202.pdf>> (1 April 2015).

Box 4: NLNG's disputes with related parties

The tax holiday case cannot be seen in isolation from a number of other disputes in which NLNG is involved with related parties in Nigeria on financial and tax issues:

- ❑ A lawsuit against NLNG was started by the Nigerian Maritime Administration and Safety Agency (NIMASA), regarding a levy of 3% of gross freight on NLNG's outbound international cargos.¹ NLNG claims that this levy is not applicable because of provisions under the NLNG Act, since it is not an income tax but a levy, from which the company is continuously exempted by sundry provisions of the NLNG Act.² In July 2013 it was reported by Nigerian newspaper The Nation that "both parties had reached an amicable settlement and that NLNG has paid US\$ 20million out of the total sum of USD 158million".³ NLNG Management claims that "Since (the expiration of the tax holiday in 2009), NLNG has been faithfully paying taxes to the Federal Inland Revenue Service, and all other relevant government bodies".⁴
- ❑ A Federal High Court judgment in 2012 pronounced a specific provision of the Nigeria LNG Act unconstitutional. In this case the Niger Delta Development Commission (NDDC), a body set up to develop the Niger Delta area, had filed an action against Nigeria LNG Ltd. seeking payment of certain charges in accordance with the law that obliges oil and gas companies to contribute to community development in the Niger Delta. This law provides that "any oil producing company operating onshore and offshore in the Niger-Delta area; including gas processing companies" shall pay 3% of its total annual budget to the body. The NDDC filed the suit against Nigeria LNG Ltd following its refusal to make this payment.⁵ In April 2012 it was announced by NLNG's lawyer that NLNG had won the court case against NDDC and that the NLNG Act should not have been declared unconstitutional.⁶ In 2014, a statement was made by NLNG claiming that "this levy is inapplicable to NLNG, a position which has the backing of decisions of the entire spectrum of courts in Nigeria, culminating in a Supreme Court ruling delivered in October 2011".⁷

1 Ibid.

2 NLNG, undated, "NLNG and NIMASA – Stating the facts," <http://www.nlng.com/publications/NLNG_NIMASA_ADVERTORIAL.pdf> (21 August 2013).

3 The Nation, "Court adopts NIMASA, NLNG settlement terms," 2013, <<http://thenationonline.ng/new/court-adopts-nimasa-nlng-settlement-terms/>> (15 July 2015).

4 Op. cit., NLNG, undated.

5 B. Adaralegbe, "Stabilizing fiscal regimes in long-term contracts: Recent developments from Nigeria, 2008," *Journal of World Energy Law & Business* (2008) 1(3):239–246.

6 Babalakin & Co. website, "NDDC wins much celebrated case against NLNG at the Supreme Court," 2012, <http://babalakinandco.com/news_nddc.htm> (18 October 2012); contrary to what the title suggests, in the article the opposite is being reported, i.e. NLNG celebrating victory over NDDC.

7 This Day Live website, 4 June 2014, NDDC Levy is Inapplicable to Nigeria LNG; <<http://www.thisdaylive.com/articles/nddc-levy-is-inapplicable-to-nigeria-lng/180152/>> (15 July 2015).

◉ **Box 4: NLNG's disputes with related parties**

- ◻ An investigation by the Petroleum Revenue Special Task Force⁸ into Nigeria's oil and gas industry has revealed the extent of mismanagement and corruption that is costing Nigeria billions of dollars each year.⁹ The Task Force, headed by former anti-corruption chief Nuhu Ribadu, revealed in its report that losses of revenue to the treasury over apparent gas price-fixing involved dealings between Total, Eni and Shell and government officials. The report does not suggest the companies broke the law but called for measures to be put in place to ensure all transactions are more transparent. The Ribadu Task Force observed that the price at which liquefied natural gas is sold to NLNG "seems too generous, compared to prices obtainable on the international market. The estimated cumulative total of the deficit between value obtainable on the international market and what is currently being obtained from NLNG, over the 10-year period, amounts to approximately US\$29 billion".¹⁰ However, it should be noted that the report has only been published as a draft and is disputed by certain stakeholders in Nigeria. In an initial reaction to the publication of the draft report, a Shell spokesman stated that "We have not seen this report and are, therefore, unable to comment on the content, but we will study it if and when it is published".¹¹

8 Report of the Petroleum Revenue Special Task Force, 2012; <https://www.premiumtimesng.com/docs_download/Report_of_the_Ribadu_led_Petroleum%20Revenue%20Special%20Task%20Force%202012.pdf> (15 July 2015).

9 BBC News Africa, "Nigeria, Oil-gas sector mismanagement costs billions," 25 October 2012, <http://www.bbc.co.uk/news/world-africa-20081268> (15 July 2015).

10 It should be noted that there is considerable controversy about the report in Nigeria. A draft version of the report was apparently leaked to the media and doubts have been raised about the accuracy of information and findings contained in the report.

11 Reuters, "Exclusive: Nigeria loses billions in cut price oil deals – report," 2012, <<http://www.reuters.com/article/2012/10/24/us-nigeria-oil-idUSBRE89NOVV20121024>> (15 July 2015).

Criticism of the 10-year tax holiday is expressed by FIRS, the Nigerian tax authority (see Figure 6). In a FIRS newsletter, July 2012, the then FIRS Director of Oil and Gas, Mr Bamidele Ajayi, stated that *"the pioneer status enjoyed by NLNG was the government's initiative to encourage the liquefied gas industry at inception. The reasoning then was that government thought Nigeria had more potentials in gas than crude, so the thought then was that they needed to develop it, and in doing so, they were given a tax holiday of 10 years, which is abnormal. However, upon the expiration of the tax holiday in 2009, it has been difficult to get them to clear up tax liabilities because of the complex clauses in the tax holiday document which made it an open-ended document."*¹⁷⁵

175 FIRS, "NLNG Has Enjoyed 10 years abnormal tax holiday" – D/Oil & Gas, 2012, <<http://www.firs.gov.ng/Resource-Centre/Documents/Newsletter%20July%202012%20Vol.%202.pdf>> (15 July 2015).

In the NLNG Annual Accounts 2011 it was reported that NLNG was involved in discussions around the payment of taxes with the Federal Inland Revenue Service. This is related to the use of certain expenses (more specifically for the lease of vessels through the Bermuda subsidiary of NLNG) that allowed NLNG to build up the high stock of deferred tax assets.¹⁷⁶ In this respect, an important development is that the NLNG Annual Accounts 2013 state that *“After a series of engagement sessions between NLNG and FIRS teams, a MoU containing the settlement agreement between NLNG and FIRS on various tax issues was signed on 4 of October 2013. Consequently the payment of US\$ 148.6 million was made by NLNG in full and final settlement of all the tax liabilities in relation to VAT, CIT, EDT, Capital Gains Tax and WHT arising from the pioneer period tax audit of NLNG.”*¹⁷⁷ It is assumed that this settlement relates to all disputed tax payments during the 10-year pioneer period, which implies that NLNG and its shareholders are paying only a fraction of what they would have paid as a normal pioneer company, as explained in section 4.3.

4.3 The potentially lost tax to Nigeria resulting from the NLNG 10 year tax holiday

When the NLNG Act was passed in 1990, Nigerian tax law already had a ‘pioneer status’ category for companies in certain industries, for which NLNG would probably have qualified, as explained in section 4.2. The criticism of the NLNG Act therefore lies in the difference between the provisions of the NLNG Act and the benefits of pioneer status, which gives new companies a tax exemption for three or five years. NLNG’s first five years of tax exemption could have been obtained through the normal pioneer status, and given that the losses and capital allowances are still carried forward, the overall tax exempt status would have most likely also been longer than five years. Had NLNG been considered a normal pioneer under Nigerian law, and the NLNG Act not created specifically for this consortium, the firm would have started to offset deferred taxes against its taxable profits in 2004, and as a result may not have paid any cash tax in that year and in the two subsequent years, 2005 and 2006, following the end of the actual tax holiday. In that case, NLNG would have had an effective tax-exempt status of 7 years instead of the present 12 years.

Based on publicly available data provided by NLNG, SOMO has calculated the amount of potentially foregone tax revenues to the Nigerian government through the extended 10-year tax holiday (as established under the NLNG Act¹⁷⁸), in comparison to what would have been received under the ‘normal’ five-year tax holiday (which any other company in Nigeria would receive under the Industrial Development (Income Tax Relief) Act 1971¹⁷⁹). We have assumed that, in both cases, deferred tax assets are carried forward after the end of the tax holiday. By making this comparison, it is possible to provide an estimate of the potentially lost tax to the Nigerian government. To be able to do so, we have quantified to what extent the tax holiday provided to NLNG has been beneficial to the three foreign shareholders, Shell, Total and Eni.

176 NLNG Annual Accounts 2011, p.26.

177 NLNG Annual Accounts 2013, p.39.

178 For full text see <http://www.placng.org/new/laws_of_nigeria3.php?sn=347>.

179 For full text see <http://www.placng.org/new/laws_of_nigeria3.php?sn=203>.

SOMO's calculation is based on the following six steps (as explained in more detail in Annex 2, especially Table A1 and A2):

□ Step 1: Basis for tax calculations

The starting point of the calculations is the profit before taxation, taken from NLNG's financial statements. As a starting point and to ensure that there is consistency in the data used, we have based our calculations on the stated profit before tax figure in each year following the normal tax holiday period of five years; this means that our calculations are made for two distinct periods:

- 2005-2009 (the five years following the 'normal' tax holiday period of five years);
- 2010-2013 (the four years following the extended tax holiday of 10 years).

To calculate the hypothetically paid tax under a five-year tax holiday, we have subtracted the income from foreign subsidiaries received from the profit before tax, which provides the basis for the tax calculations that follow. The reason for subtracting the income from foreign subsidiaries received is that this is also exempted from tax according to the NLNG Act.¹⁸⁰

□ Step 2: Calculation of corporate income tax (CIT)

In Step 2 we have applied a corporate income tax rate (CIT) of 30% to the tax base, as this is the rate that NLNG reports for 2011 and beyond. In the years 2005 and 2006, NLNG would in this case still be eligible for carrying forward unused deferred tax assets from previous years, as indicated under 'Adjustments under Standard 5 year tax holiday'. This means that in 2005, and partly in 2006, income tax is offset against deferred tax assets. In our hypothetical calculation, deferred tax assets are not relevant after 2006, as all deferred tax assets have already been used to lower profit before tax by the end of 2006 (as can be seen in Annex 2, Table A1). This leads to the potential CIT lost as calculated in the same table for the years 2005 to 2013.

□ Step 3: Calculation of education tax

In Step 3 we calculated the education tax (2% of tax before profits) potentially lost as it would have been payable in the case of a five-year 'normal' tax holiday. Since between 2010 and 2013 education tax was paid/payable according to the financial statements, we excluded those years from the total. This leads to a potentially lost education tax of US\$ 276 million for the years 2005 to 2009. It should be noted that the education tax calculated in our calculations differs from the education tax as calculated in the company's annual accounts, which is probably due to accounting differences related to our hypothetical situation.

□ Step 4: Calculation of total potentially lost tax

In Step 4 we have added the potentially lost corporate income tax to the education tax, leading to a cumulative lost tax of around US\$ 7.7 billion during the nine-year period 2005-2013. From this amount we have deducted the deferred tax liability of US\$ 1.15 billion that appears on the

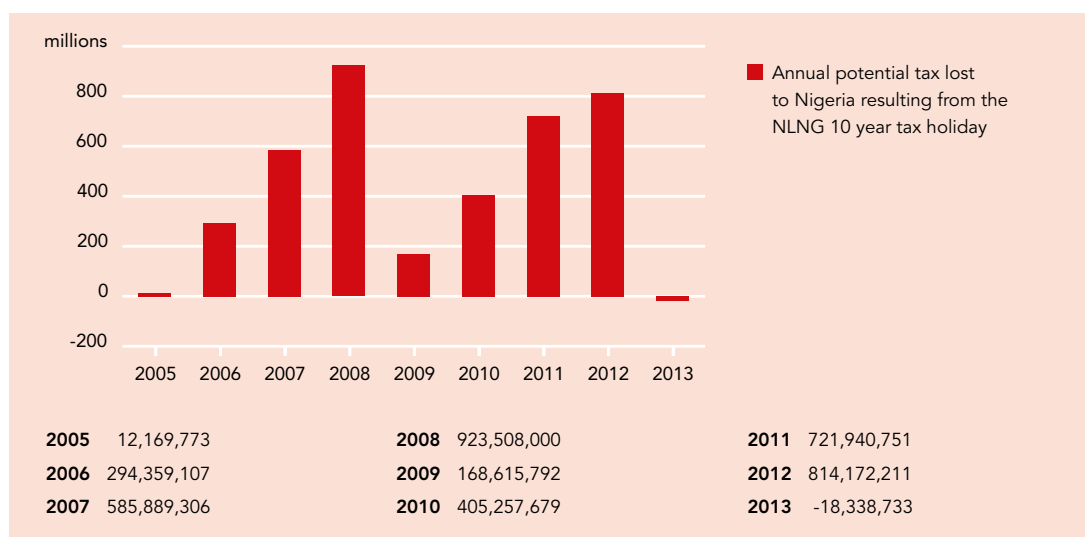
¹⁸⁰ Under normal circumstances, this would be justifiable as this dividend would have been taxed in the country where the profits were made. However, in the case of NLNG, the major share of the dividends is made through Bonny Gas Transport, based in Bermuda, where the income tax rate is 0%.

company's balance at the end of 2013, as a result of the deferred tax payments in 2012. This leads to a total cumulative lost tax of around US\$ 6.5 billion.

Step 5: Calculation of total potentially lost tax to the Nigerian government from unpaid taxes by the three foreign shareholders

In Step 5 we have calculated the amount of potentially lost tax to the Nigerian government by taking into account the fact that NLNG is a joint venture between the Nigerian oil corporation, NNPC (49% share), Shell (25.6%), Total (15%) and ENI (10.4%). Therefore, based on the Nigerian government's interest of 49% in NLNG, we have multiplied the total amount of foregone tax by 0.51 to arrive at the potential amount of tax lost to the Nigerian treasury. As can be seen in Annex 2, Table A1, this leads to a total tax loss to the Nigerian government of around US\$ 3.3 billion over a period of nine years (2005-2013) or around US\$ 369 million per year. See also Figure 7 below.

Figure 7: Calculations of annual potentially lost tax to the Nigerian government due to NLNG under a five-year tax holiday, based on a 51% share of the three oil companies (in US\$)¹⁸¹



Source: SOMO, based upon data directly obtained from the Annual Reports of Nigeria LNG Ltd (2007-2013).

Note: All figures are given in US\$.

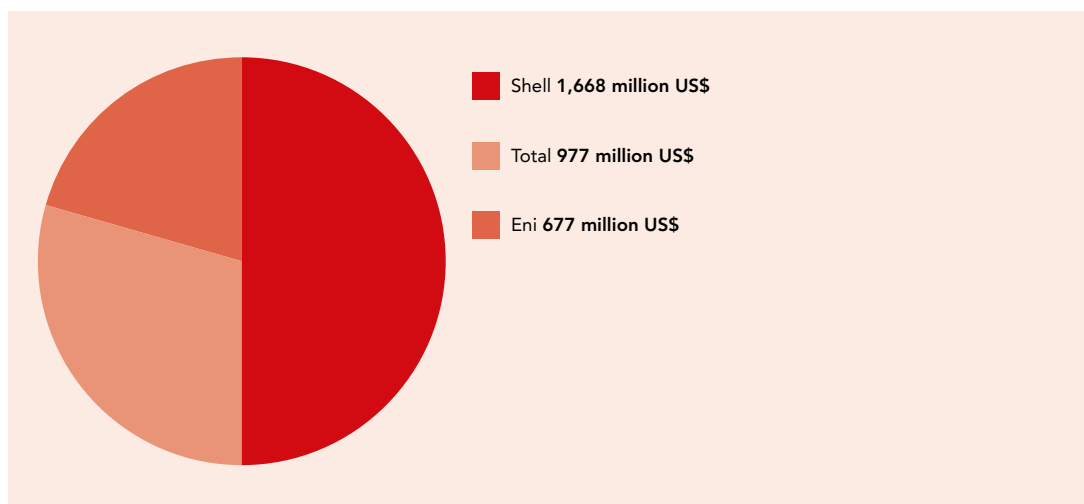
Step 6: Attribution of tax potentially lost to the Nigerian government from unpaid Shell, Total and Eni taxes

Based on Shell's share of 25.6%, the tax lost to the Nigerian government directly attributable to Shell amounts to around US\$ 1.7 billion over a period of nine years. The tax lost to the Nigerian

181 Calculations by author.

government directly attributable to Total amounts to around US\$ 977 million over a period of nine years, while for Eni the tax lost amounts to around US\$ 677 million over the same period. This is reflected in Annex 2, Table A2.

Figure 8: Share of potentially lost tax to the Nigerian government directly attributable to the three companies over the period 2005 - 2013¹⁸²



The estimate of US\$ 3.3bn cost to the Nigerian government is a conservative estimate. First, the calculations only include lost tax revenues from the three private companies' share of the joint venture; 51% of the total. Second, it only calculates lost tax revenues from two taxes: corporate income tax and education tax. It excludes all other taxes exempted under included in the tax holiday, such as the NDDC tax¹⁸³, tax on profits from subsidiaries, and custom duties. Third, at the end of 2013 US\$1.15bn was still owed to the Nigerian government as tax obligations from 2012.

¹⁸² Calculations by author.

¹⁸³ As stated in Box 4, the Niger Delta Development Commission (NDDC) filed a suit against NLNG following its refusal to make the payment of taxes for local development of the Niger Delta, based on the argument that exemption from this tax is also part of the 10-year tax holiday. In 2014 it was reported by NLNG that it had won the court case against NDDC. Even though this could not be confirmed by independent sources, in the interests of prudence we have not included the hypothetical lost NDDC tax in our calculations.

5 Conclusion

SOMO has calculated the tax income potentially lost to the Nigerian government as a result of the extended 10-year tax holiday from which Shell, Total and Eni have benefited through their joint venture, Nigeria LNG Company – in which these companies share a majority stake (51%). The 10-year tax holiday was granted through a law called the NLNG Act – an act created specifically for Nigeria LNG – as all other new companies investing in Nigeria are given a tax exemption grace period of ‘just’ three to five years.

This tax break, and the application of other legal provisions (for example, the carrying forward of deferred tax assets), reduced NLNG’s tax bill to almost zero for a total of 12 years. The total tax potentially lost in this way to the Nigerian government amounts to a staggering US\$ 3.3 billion during the period of 2005 to 2013 – an average lost tax of around US\$ 369 million per year.¹⁸⁴ This is especially relevant in the context of a country where more than half of the population lives below the poverty line that could have benefited enormously from these foregone tax payments.

These calculations take account of the fact that the Nigerian government has a 49% stake in NLNG, which means that part of the tax lost theoretically flows back into the Treasury, although it is unclear through which channels. In other words, the calculations in this report are limited to the private companies’ stake in the business, or 51% of the foregone tax, which was lost to the Nigerian government. As shown in this report, tax potentially lost to the Nigerian government which is directly attributable to the three companies can be broken down as follows:

- For Shell, based on its 25.6% interest in NLNG, this amounts to around US\$ 1.7 billion.
- For Total, based on its 15% interest in NLNG, this amounts to US\$ 977 million.
- For ENI, based on its 10.4% interest in NLNG, this amounts to US\$ 677 million.

In Nigeria, so far, no other companies have benefited from a similar extended tax holiday enacted by law. However, recently a bill to amend the Companies Income Tax Act was passed at the Nigerian National Assembly. The proposed amendment aims to provide additional tax incentives for gas utilization, mining sectors and businesses located in areas with inadequate infrastructure and includes an extension of the period for tax holidays to 10 years for all companies operating in Nigeria.

This bill is expected to lead to even fewer foreign companies paying their fair share of taxes in Nigeria, a country that already has a problem in ensuring sufficient domestic revenue mobilization from the private sector and from ordinary citizens. As a consequence of this new bill, the only substantial source of taxation – taxes on companies extracting Nigeria’s natural resources – will be seriously eroded and foreign companies will be allowed to benefit from tax breaks as massively as the three oil companies in this case study did.

¹⁸⁴ This is the total potential tax lost to the Nigerian government for all three companies together, comprised of non-paid corporate income tax and education Tax. No financial data were available for the years 1999–2004, so the loss is potentially even higher.

Key conclusions and recommendations

- ❑ Royal Dutch Shell, Total and Eni, as majority owners of the joint venture Nigeria LNG (51%), are exploiting natural liquefied gas in Nigeria at a bargain price due to an extended 10-year tax holiday – a tax break double what any other company was given when starting a business in Nigeria. In addition, due to other legal provisions including the carrying forward of deferred tax assets, the company's tax bill was reduced to almost zero during these 12 years, instead of the standard period of 5 years.
- ❑ SOMO's calculations show that this tax holiday has been extremely costly for Nigeria, but very beneficial for the three private sector partners in the NLNG venture. The tax incentive, which became law through an act of parliament, appears in principle to have been subject to democratic scrutiny though there is no information regarding whether the three companies Shell, Total, and Eni influenced the enactment of the NLNG Act. It is however doubted whether the NLNG Act has been beneficial for Nigeria, given the high amounts of tax potentially lost to the Nigerian government.
- ❑ This case study provides a clear illustration of the negative economic impacts of tax breaks given to foreign companies in oil- and gas producing developing countries. The Nigerian government's use of very generous tax breaks – and the willingness of multinational companies to use these tax breaks – needs to be questioned as it has been shown to have harmful impacts on governments and citizens in the host countries.
- ❑ There is no account publicly available on how the Nigerian government (a 49%-shareholder in NLNG) has spent its share of the dividends. NLNG's total profits amounted to at least US\$ 29.5 billion over the period 2004 to 2013. In Nigerian Extractive Industries Transparency Initiative (NEITI) audits, questions have been raised about who actually benefits from NLNG's operations: the Nigerian federation, the federal government, or the Nigerian state oil corporation (NNPC) itself?
- ❑ The Nigerian government is demanded to provide more clarity on how this extended tax holiday and the NLNG Act came into being, and on the reasoning behind the granting of a 10-year tax holiday instead of the standard five-year period in Nigeria.
- ❑ The Nigerian government is demanded to:

 - publish any costs-benefit analysis or arguments behind the NLNG Act and publicly explain the reason behind the ten-year tax holiday to the Nigerian people;
 - make a cost-benefit analysis of current tax incentives granted to the Consortium and propose to change the Act as appropriate.

- The Nigerian Parliament is demanded to:

 - revoke the proposed amendment to the Companies Income Tax Act, which aims to extend pioneer status tax holidays from 5 to 10 years;
 - investigate the process that led to the NLNG Act, and make the findings known to the Nigerian public;
 - demand that the executive arm of government follows up on the previous government's statement of intent to review the tax incentive practices in Nigeria.

- Given their corporate responsibility to provide revenue transparency, it is demanded from Shell, Total and Eni to publicly disclose information on sales, the number of employees, profits made and taxes paid in Nigeria, in line with the country by country reporting template¹⁸⁵ proposed as part of the base erosion and profit shifting (BEPS) process.¹⁸⁶ It is demanded that companies publish their accounts from all subsidiaries in Nigeria on their website and make public what they gain from the various tax incentives enjoyed in Nigeria every year. Only by publishing these data will governments, parliaments and citizens know how much the Nigerian public is positively or negatively affected by the three companies in Nigeria. It is also demanded from the three companies that they pay taxes at prevailing rates without seeking tax incentives in developing countries as a requirement to establishing businesses there, and seek a level tax playing field with other corporate taxpayers, domestic and multinational, in all jurisdictions where they operate.

- As host states of the three multinational companies, it is demanded that the governments of Italy, the Netherlands, France and the UK require that companies registered under specific country legislation report and publicly disclose information on sales, the number of employees, profits made and taxes paid in each country and jurisdiction in which they operate. In promoting international trade/business/investments, resident governments must not engage in political or other activities that will lead to the private sector organisations being offered excessive and harmful tax incentives in other countries.

- This case study has focused on the overgenerous tax breaks awarded to Nigeria LNG. In addition, it would be interesting to investigate a number of other aspects that raise questions about this company, especially the fact that one of NLNG's wholly-owned subsidiaries, Bonny Gas Transport Ltd, is based in Bermuda, a notorious tax haven. It was beyond the scope of this report to look into this case, but it is recommended to do follow-up research on the Bermuda connection of NLNG.

185 Country by country reporting obliges companies to publish key financial data for each country in which they operate.

186 Base Erosion and Profit Shifting project of the OECD.

Annex 1

NLNG shareholders



Nigerian National Petroleum Corporation (NNPC)

Nigerian National Petroleum Corporation was established in 1977 under the laws of the Federal Republic of Nigeria. It is the corporate entity through which the Nigerian government participates in the oil and gas industry. NNPC and its subsidiaries dominate all sectors of the industry—exploration, production, refining, pipelines, marketing, crude/product exports, and petrochemicals. NNPC owns 49% of the shares in Nigeria LNG Limited



Shell Gas B.V. (SGBV)

Shell Gas B.V. (SGBV) is a company incorporated under the laws of the Netherlands. For more than 40 years, Shell Gas has been investing in and delivering some of the world's largest and most complex gas projects. Besides its interest in Nigeria LNG Limited, Shell Gas holds the largest equity share of LNG capacity among international oil companies, with a leading position in LNG shipping, marketing and trading of natural gas and power in Europe, North America and Asia Pacific. It is a member of the Royal Dutch Shell Group of Companies which operates throughout the world in all subsectors of the petroleum industry. SGBV owns 25.6% of the shares in Nigeria LNG Limited.



Total LNG Nigeria Limited

Total is a major integrated oil and gas company active in all sectors of the petroleum industry. It operates in more than 130 countries, and is, today, the fifth largest publicly traded integrated international oil and gas company in the world. In Nigeria, the company is one of the largest oil and gas producers through its involvement in more than 50 permits, including nine as operator. Total owns 15% of the shares in Nigeria LNG Limited.



Eni International (N.A.) N.V.S.a.r.l

Eni is one of the world's major integrated oil and gas companies engaged in all sectors of the petroleum business. It is involved in exploration, development and production of oil and natural gas in 70 countries. Eni owns 10.4% of the shares in Nigeria LNG Limited.

Source: Nigeria LNG, 2015, facts and figures on NLNG 2015, p.9; <http://www.nlng.com/Media-Center/Publications/Facts_and_figures_2015.pdf>.

Annex 2

Calculations for the NLNG case study: detailed explanations

This annex includes detailed explanations of the calculations for the potentially lost tax in the NLNG case study in this report. The calculations are presented in Table A1.

Based on publicly available data provided by NLNG we calculated the amount of potentially foregone tax revenues to the Nigerian government through the extended (10-year) tax holiday (as established under the NLNG Act¹⁸⁷), in comparison to what would have been received under a 'normal' five-year tax holiday (as any other company in Nigeria would receive under the Industrial Development (Income Tax Relief) Act 1971¹⁸⁸). We have assumed that, in both cases, unused tax losses are carried forward after the end of the tax holiday.

By making this comparison, it is possible to provide an estimate of the tax potentially lost to the Nigerian government. To be able to do so, we have quantified to what extent the tax holiday provided to NLNG has been beneficial to the three foreign shareholders, Shell, Total and Eni. A calculation has been made specifying the amount of potentially lost tax to the Nigerian government as a result, which is explained for each step below (see also Table A1 and A2).

More specifically, we have assumed that NLNG would have been eligible for a tax relief under the Industrial Development (Income Tax Relief) Act 1971, which stipulates that pioneer companies are exempted from taxes imposed by the government (including exemption from income tax) for a period of a minimum three and maximum of five years. Therefore, it is assumed that no income tax or other taxes are due during the first five years (1999-2004 for the NLNG case). Assuming that after the initial five-year period no tax relief is applicable, for subsequent years (2005 onwards) an income tax rate of 30% applies.¹⁸⁹ This is based on the information provided in the 2009 annual accounts of NLNG in which an income tax rate of 30% is provided¹⁹⁰ and it is also in line with the Nigerian business tax regulations, in which a corporate income tax rate of 30% applies.¹⁹¹

Step 1: Basis for tax calculations

Starting point of the calculations is the profit before taxation, taken from NLNG's Financial Statements. As a starting point and to ensure that there is consistency in the data used, we have based our calculations on the stated profit before tax figure in each year following the normal tax holiday period of 5 years; this means that our calculations are made for two distinct periods:

187 For full text see <http://www.placng.org/new/laws_of_nigeria3.php?sn=347>.

188 For full text, see <http://www.placng.org/new/laws_of_nigeria3.php?sn=203>.

189 Compared to 85% petroleum profit tax for oil companies.

190 NLNG Annual Accounts 2009, p.20.

191 Ernst & Young, "Worldwide corporate tax guide – Nigeria," 2015, <<http://www.ey.com/GL/en/Services/Tax/Worldwide-Corporate-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/WCTG-2014/WCTG-NG.xml>> (15 July 2015).

- 2005-2009: the 5 years following the “normal” tax holiday period of 5 years;
- 2010-2013: the 4 years following the extended tax holiday of 10 years.

To calculate the hypothetically paid tax under a 5-year tax holiday, we have subtracted the dividends received from the profit before tax, which provides the basis for the tax calculations that follow. The reason for subtracting the dividends received is that this is also exempted from tax according to the NLNG Act.¹⁹²

Step 2: Calculation of corporate income tax (CIT)

In Step 2, we have applied the CIT of 30% to the tax base, as this is the corporate income tax rate that NLNG is reporting in 2011 and beyond. In the years 2005 and 2006, NLNG would in this case still be eligible for carrying forward unused deferred tax assets from previous years, as indicated under “Adjustments under Standard 5 year tax holiday”. This means that in 2005, and partly in 2006, income tax is offset against deferred tax assets. In our hypothetical calculation, deferred tax assets are not relevant after 2006, as all deferred tax assets have already been used to lower profit before tax by the end of 2006 (as can be seen in the table). This leads to the potentially CIT lost as calculated in the table for the years 2005-2013.

Step 3: Calculation of education tax

In Step 3, we calculated the education tax (2% of tax before profits) potentially lost as it would have been payable in the case of a 5 year “normal” tax holiday. Since between 2010 and 2013 Educational Tax was paid/payable according to the Financial Statements, we excluded those years from the total. This leads to a potentially lost education tax of US\$ 276 million for the years 2005-2013. It should be noted that the education tax calculated in our calculations differs from the education tax as calculated in the company’s Annual Accounts, which is probably due to accounting differences because of our hypothetical situation.

Step 4: Calculation of total potentially lost tax

In step 4, we have added the potentially lost corporate income tax to the education tax, leading to a cumulative lost tax of around US\$ 7.7 billion during the nine-year period of 2005 to 2013. From this amount, we have deducted the deferred tax liability of US\$ 1,15 billion that appears on the company’s balance at the end of 2013, as a result of the deferred tax payments in 2012. This leads to a total cumulative lost tax of around US\$ 6.5 billion.

Step 5: Calculation of total potentially lost tax to the Nigerian Government from unpaid taxes

In Step 5, we have calculated the amount of potentially lost tax to the Nigerian Government by taking into account the fact that NLNG is a joint venture between the Nigerian oil corporation, NNPC (49% share), Shell (25.6%), Total (15%) and ENI (10.4%). Therefore, based on the Nigerian Government’s interest of 49% in NLNG, we have multiplied the total amount of foregone tax by 0.51 to arrive at the potential amount of tax lost to the Nigerian Treasury. As can be seen in the table below, this

¹⁹² Under normal circumstances, this would be justifiable as this dividend would have been taxed in the country where the profits were made. However, in the case of NLNG, the major share of the dividends is made through Bonny Gas Transport, based in Bermuda, where the income tax rate is 0%.

leads to a total tax loss to the Nigerian Government of around US\$ 3.3 billion over a period of 9 years (2005-2013) or around US\$ 369 million per year.

Step 6: Attribution of potentially lost tax to the Nigerian Government from unpaid Shell, Total and Eni taxes

Based on Shell's share of 25.6%, the tax lost to the Nigerian Government directly attributable to Shell amounts to around US\$ 1.7 billion over a period of 9 years. The tax lost to the Nigerian Government directly attributable to oil company Total amounts to around US\$ 977 million over a period of 9 years, while for ENI the tax lost amounts to around US\$ 677 million over the same period. This is reflected in Table A2 below.

It should be noted that in the above calculation, we have not included the hypothetically lost NDDC tax. As stated in Box 4 above, the Niger Delta Development Commission (NDDC) filed a suit against NLNG following its refusal to make the payment of taxes for local development of the Niger Delta, based on the argument that exemption from this tax is also part of the 10-year tax holiday. In April 2012, it was announced by NLNG's lawyer that NLNG has won the court case against NDDC. Even though this could not be confirmed by independent sources, from a prudence perspective we have decided not to include the hypothetical lost NDDC tax in our calculations.

Table A1: Calculations of potential tax lost to Nigeria resulting from the NLNG 10 year tax holiday – step 1 to 4
All amounts in US dollars

STEP 1	Calculation Corporate Income Tax	First year income tax is paid Y14	No tax paid because of deferred tax assets Y13	No tax paid because of deferred tax assets Y12	No tax paid because of deferred tax assets Y11	No tax paid because of extended Tax Holiday Y10	No tax paid because of extended Tax Holiday Y9	No tax paid because of extended Tax Holiday Y8	No tax paid because of extended Tax Holiday Y7	No tax paid because of extended Tax Holiday Y6	Normal Tax Holiday Y5
	Financial Year	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
	Profit Before Taxation according to Financial Statements NLNG	4,509,869,000	5,321,387,000	4,884,567,000	2,798,743,000	1,313,185,000	5,841,750,000	3,804,008,000	2,334,921,000	1,193,115,000	1,003,738,000
	Dividends received	(225,000,000)	0	(166,000,000)	(150,000,000)	(280,000,000)	(183,000,000)	(214,000,000)	0	0	0
	Basis for Tax calculations	4,284,869,000	5,321,387,000	4,718,567,000	2,648,743,000	1,033,185,000	5,658,750,000	3,590,008,000	2,334,921,000	1,193,115,000	1,003,738,000
STEP 2	Calculation Corporate Income Tax	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
	Basis for Tax calculations	4,284,869,000	5,321,387,000	4,718,567,000	2,648,743,000	1,033,185,000	5,658,750,000	3,590,008,000	2,334,921,000	1,193,115,000	1,003,738,000
	Corporate Income Tax @ 30%	(1,285,460,700)	(1,596,416,100)	(1,415,570,100)	(794,622,900)	(309,955,500)	(1,697,625,000)	(1,077,002,400)	(700,476,300)	(357,934,500)	NA
	Adjustment for deferred tax assets under Standard 5 year Tax Holiday	0	0	0	0	0	0	0	170,000,000	357,934,500	not available
	Corporate Income Tax under Standard 5 Y Tax Holiday	(1,285,460,700)	(1,596,416,100)	(1,415,570,100)	(794,622,900)	(309,955,500)	(1,697,625,000)	(1,077,002,400)	(530,476,300)	0	0
	Corporate Income tax actually paid or payable	1,321,419,000	0	0	0	0	0	0	0	0	0
	Corporate Income Tax potentially lost	35,958,300	(1,596,416,100)	(1,415,570,100)	(794,622,900)	(309,955,500)	(1,697,625,000)	(1,077,002,400)	(530,476,300)	0	NA
Cumulative Corporate Income Tax potentially lost	(7,385,710,000)	(7,421,668,300)	(5,825,252,200)	(4,409,682,100)	(3,615,059,200)	(3,305,103,700)	(1,607,478,700)	(530,476,300)	0	0	
STEP 3	Calculation Education Tax	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
	Basis for Tax calculations	NA	NA	NA	NA	1,033,185,000	5,658,750,000	3,590,008,000	2,334,921,000	1,193,115,000	NA
	Education Tax @ 2%	NA	NA	NA	NA	(20,663,700)	(113,175,000)	(71,800,160)	(46,698,420)	(23,862,300)	NA
	Education tax actually paid or payable	101,783,000	118,529,000	107,047,000	65,071,000	0	0	0	0	0	0
	Education Tax potentially lost	0	0	0	0	(20,663,700)	(113,175,000)	(71,800,160)	(46,698,420)	(23,862,300)	NA
Cumulative Potentially Education Tax lost	(276,199,580)	(276,199,580)	(276,199,580)	(276,199,580)	(276,199,580)	(255,535,880)	(142,360,880)	(70,560,720)	(23,862,300)	0	
STEP 4		2013	2012	2011	2010	2009	2008	2007	2006	2005	2004
	Total Corporate Income & Education Tax potentially lost	35,958,300	(1,596,416,100)	(1,415,570,100)	(794,622,900)	(330,619,200)	(1,810,800,000)	(1,148,802,560)	(577,174,720)	(23,862,300)	NA
	Cumulative Corporate Income & Education Tax Potentially lost	(7,661,909,580)	(7,697,867,880)	(6,101,451,780)	(4,685,881,680)	(3,891,258,780)	(3,560,639,580)	(1,749,839,580)	(601,037,020)	(23,862,300)	0
	-/- Deferred tax liabilities end of 2013	1,147,695,000									
Total Corporate Income & Education Tax potentially lost	(6,514,214,580)										

Table A2: Calculations of potential tax lost to Nigeria resulting from the NLNG 10 year tax holiday – step 5 and 6

All amounts in US dollars

	STEP 5		STEP 6		
	Calculation of total potentially lost tax to the Nigerian Government		Attribution of potentially lost tax to the Nigerian Government to Shell, Total and Eni		
	Total	Total tax loss to Nigeria (51% of total)	Shell share of 25,6%	Total share of 15%	ENI share of 10,4%
Calculation Corporate Income Tax					
Corporate Income Tax potentially lost	(7.385.710.000)	(3.766.712.100)	(1.890.741.760)	(1.107.856.500)	(768.113.840)
Calculation Education Tax					
Education Tax Potentially lost	(276.199.580)	(140.861.786)	(70.707.092)	(41.429.937)	(28.724.756)
Total Corporate Income & Education Tax potentially lost	(7.661.909.580)	(3.907.573.886)	(1.961.448.852)	(1.149.286.437)	(796.838.596)
-/- Deferred tax liabilities end of 2013	1.147.695.000	585.324.450	293.809.920	172.154.250	119.360.280
Total Corporate Income & Education Tax potentially lost per year (over 9 year period 2005-2013)	(6.514.214.580)	(3.322.249.436)	(1.667.638.932)	(977.132.187)	(677.478.316)

Annex 3

Glossary¹⁹³

Arm's length price

If a transfer price can be shown to be the same as the market price (the arm's length price) then it is acceptable for tax purposes (see transfer pricing).

Associated natural gas

Natural gas that occurs in crude oil reservoirs as free gas

bbbl/day

Barrels of oil per day – a measure for the rate of production of an oil well or a production unit.

bcm

Billion cubic metres of natural gas (abbreviated: bcm) is a measure of natural gas production and trade.

BGT

Bonny Gas Transport – the Bermudan fully owned subsidiary of NLNG that transports its gas.

boe/day

Barrels of oil equivalent per day – a measure for the rate of production of an oil well or a production unit.

Capital gains taxes

A tax on the profits from the disposal of capital assets such as stocks and shares, land and buildings, businesses, and valuable assets such as works of art.

CIT

Corporate income tax. See: Corporate taxes

Corporate taxes

Taxes on the profits made by limited liability companies and other similar entities. The tax is generally imposed on net taxable income, specified in the company's financial statement, but corrected for divergences between commercial and tax calculation of profit.

Country-by-country reporting

A proposed accounting standard under which a multinational corporation would be required to report key financial information in its annual accounts for each country and territory in which it operates.

193 This glossary is based largely on the Toolkit for Tax Justice, see <<http://taxjustice.somo.nl/>>.

Deferred tax

Deferred tax assets are tax credits, for example related to current losses, which the company can offset against future tax liabilities.

Dry natural gas

Natural gas which remains after: 1) the liquefiable hydrocarbon portion has been removed from the gas stream (i.e., gas after lease, field, and/or plant separation); and 2) any volumes of nonhydrocarbon gases have been removed where they occur in sufficient quantity to render the gas unmarketable. Note: Dry natural gas is also known as consumer-grade natural gas.

EITI

Extractive Industries Transparency Initiative – a multi-stakeholder initiative for transparency in the extractives sector.

Excise taxes

These are taxes usually imposed on a limited range of goods, such as luxury goods, or on products that can have a harmful impact on the consumer.

FIRS

Federal Inland Revenue Service – the Nigerian tax authority.

Income tax

Taxes on income, profits, inheritance, payroll and capital gains are generally divided between taxes payable by individuals and corporations.

JV

Joint venture – a company jointly owned and governed by two or more companies or governments, such as NLNG. In the oil and gas sector, joint ventures usually have a single operator, for practical reasons, which in the case of NLNG and Shell Petroleum Development Company of Nigeria is Shell.

NDDC

Niger Delta Development Commission – a Nigerian federal government agency with the task of developing the oil-rich Niger Delta socially and economically.

NEITI

Nigerian Extractive Industries Transparency Initiative, see EITI.

NNPC

Nigerian National Petroleum Company – the Nigerian state company for the oil and gas sector.

NLNG

Nigeria LNG – a joint venture between the Nigerian government (49%), Shell (25,6%), Total (15%) and ENI (10,4%), which produces liquefied natural gas at the Bonny Island gas plant in Nigeria.

OPEC

Organization of Petroleum Exporting Countries – a group of oil-rich countries that attempts to cooperate in setting production amounts in an effort to control prices.

OPL

Oil producing licence – a concession to explore and mine a certain area for fossil fuels.

PSC

Production sharing contract, see Figure 2, section 4.2: The tax system in the Nigerian oil and gas industry.

PWYP

Publish What You Pay – a global network of civil society organisations campaigning for transparency in the extractive industries.

PPT

Petroleum profit tax, the Nigerian form of income tax for oil and gas companies.

Royalties

Royalties are usage-based payments for ongoing use of an asset as prescribed in a license agreement, for example natural resources such as oil, minerals, fisheries and forests, but also intellectual property including music and pharmaceutical products. Royalties are typically agreed upon as a percentage of revenues raised from the use or gradual depletion of an asset.

SCF

Standard cubic feet – a volume measure commonly used in the gas industry.

SEC

Securities Exchange Commission – the US oversight body for the financial sector.

Secrecy jurisdiction

Secrecy jurisdictions are countries and territories that provide financial secrecy that undermines the regulation of another jurisdiction for the primary benefit and use of those not resident in their geographical domain.

SEPA

Shell Exploration and Production Africa Limited – a Nigerian Shell subsidiary which is paid for technical advice and other intangible services by Shell subsidiaries all over Africa.

SGSI

Shell Global Solutions International – a Dutch Shell subsidiary which is paid for technical advice and other intangible services by Shell subsidiaries all over the world.

SIEP

Shell International Exploration and Production – a Dutch Shell subsidiary which is paid for technical advice and other intangible services by Shell subsidiaries all over the world.

SNEPCo

Shell Nigerian Exploration and Production Company Limited – one of the main Shell subsidiaries in Nigeria.

SPDC

Shell Petroleum Development Company of Nigeria – the main Shell subsidiary in Nigeria.

Tax

A fee levied by a government or a regional entity on a transaction, product or activity in order to finance government expenditure. Tax rates and the tax base are decided by a representative legislative body, based on constitutional provisions.

Tax avoidance

The term given to the practice of seeking to minimize a tax bill within the letter of the law (as opposed to illegal methods that would be classed as tax evasion or fraud). This often involves manipulating the tax base to minimise tax payable.

Tax dodging

A legally imprecise term that is often used by tax justice campaigners when it is not clear whether tax is being avoided or evaded. It highlights the fact that many tax avoidance strategies are abusive, while being considered legal.

Tax evasion

A term used to denote illegal methods used to pay less tax. Also known as tax fraud.

Tax haven

See 'secrecy jurisdiction'.

Tax holiday

A period during which a company investing in a country does not have to pay tax under an agreement with the government.

Tax incentives

A tax incentive is an aspect of the tax code designed to encourage a certain type of behaviour. This may be accomplished through means such as limited periods of tax holidays or permanent tax deductions on certain items.

Tax planning

When tax legislation allows more than one possible treatment of a proposed transaction, the term may legitimately be used for comparing various means of complying with taxation law.

Trade mispricing

The term used to cover both transfer mispricing and false invoicing.

Transfer pricing

A transfer-pricing arrangement occurs when two or more businesses that are owned or controlled directly or indirectly by the same group trade with each other. If a transfer price can be shown to be the same as the market price (the arm's length price) then it is acceptable for tax purposes.

Transfer-pricing abuse

This involves the manipulation of prices of transactions between subsidiaries of multinationals, or, more specifically, the sale of goods and services between affiliated companies within a multinational corporation at artificially high or low prices (outside the arm's length range). This may occur for a number of reasons, including to shift profits to low-tax jurisdictions or countries providing preferred tax treatment to certain types of income (can also be referred to as 'transfer mispricing').

Value added tax (VAT)

A tax charged by businesses on sales and services but which allows businesses to claim credit from the government for any tax they are charged by other businesses in the production chain. Different from the general services tax, which does not require proof of being an intermediate producer. VAT is often criticised for being regressive.

Withholding tax

Tax deducted from a payment made to a person outside the country. Generally applied to investment income, such as interest, dividends, royalties and licence fees according to a double tax treaty (DTT) signed between the two jurisdictions.

Annex 4

Company responses to the draft report

As part of SOMO's research process, the four shareholders of the joint venture, NNPC, Shell, Total and Eni, as well as NLNG management, have been given the opportunity to review the draft report, notify us of any factual misunderstandings and provide us with additional information. They were also asked to provide specific responses to a number of questions. In this annex, the letter by SOMO and ActionAid to the companies is provided. This is followed by a description of the way in which the three foreign shareholders as well as NLNG management have responded to the initial findings. No response was received from the Nigerian National Petroleum Corporation (NNPC).

Letter from SOMO and ActionAid to the three foreign shareholders

<Name and address of company>

RE: Request for reviewing draft report

Amsterdam, 16 September 2015

Dear <name of the addressee>,

On the 4th of September 2015, ActionAid and SOMO informed you about our intention to send you part of the draft report in which <name of company> is mentioned for review. As a standard element in SOMO's research procedure, before publishing our findings, we would like to allow you the opportunity to review the draft report, notify us of any factual misunderstandings and provide us with additional information. ActionAid and SOMO's goal is to publish complete and accurate information about your company. In addition we kindly request you to answer the following questions;

- ❑ Throughout our research for this report, ActionAid and SOMO have struggled to find any publicly available information about how and why the NLNG Act provided the NLNG with a 10 year tax holiday rather than the customary 5 year tax holiday that companies qualifying for pioneer status would be expected to get. Could <name of company> please clarify the reasons for why you were given this tax holiday, and what contacts yourself and representatives for <name of company> and the NLNG had with the Nigerian authorities before the signing of this law. Getting additional information from yourself on this will help ensure our report can convey what happened as accurately as possible.
- ❑ In our research, we have also come across conflicting information regarding what royalty payment requirements NLNG is subject to. Our understanding that royalties are normally not paid on gas sales in Nigeria and that indeed NLNG has not made any royalty payments. The latest available Nigerian EITI audit that was published in 2015 does however indicate that gas royalty rates in Nigeria are 7% for onshore and 5% for offshore operations. Could you please confirm which royalty rate you consider NLNG to be subject to and how much royalty payments the NLNG has made to the Nigerian state since operations started?
- ❑ Our understanding of NLNG's accounts is that a tax liability of US\$1.15bn payable in 2012 has been deferred. Could you please clarify the circumstances of that deferral and give any information on whether you intend to make that payment within the foreseeable future?
- ❑ Can you confirm whether or not NLNG is subject to any taxes in Nigeria on its dividend income from Bonny Gas Transport Ltd and Nigeria LNG Ship Manning Limited and whether such taxes have been paid? Are either of those companies subject to taxation in any other jurisdiction and if so what taxes have been paid so far?

The standard review period is two weeks. We therefore kindly ask you to send us any comments on the draft report and provide us with answers to the list of questions latest September 30th 2015. After having incorporated your relevant comments and answers to our questions, the report will be published on the websites of ActionAid (www.actionaid.org) and SOMO (www.somo.nl).

Please send your reaction to <email address>.

We hope that you will be able to reserve some time in your agenda to review the draft report and to answer our questions. If you have any questions about the research or the review process, please do not hesitate to contact us at the email addresses below.

Thank you in advance for your cooperation.

Yours sincerely,

How the companies responded to our findings

Below, a brief description is provided of the way in which the three foreign shareholders as well as NLNG management have responded to the initial findings. The findings have also been sent for review to the Nigerian National Petroleum Corporation (NNPC), which holds the 49% share on behalf of the Nigerian Government, but no response was received.

□ Response by Royal Dutch Shell

In a letter dated 7 October 2015, a representative of Royal Dutch Shell is responding that NLNG is an independent company and that we should refer to NLNG for a reaction to the report. In addition, Shell is providing general information about its business principles and tax affairs, and refers to the 2014 Shell Sustainability Report and the 2014 payments to governments' disclosure on its website.

□ Response by Total

On 30 September 2015, a representative of Total provided a brief response to the report in a telephone conversation. Among others, he stated that most of the questions raised in our letter only indirectly concerned Total, as the joint-venture was in Nigeria. In an email dated the same day (30 September 2015), the company provides a response to one of the questions raised

□ Response by ENI

In an email dated 30 September 2015, ENI responded extensively to our letter, providing answers to the four questions raised. ENI then continues with a list of comments to the part of the draft report dealing specifically with Eni (section 2.3), which have been used to complete the company profile of ENI in the final version of the report. The letter also includes a general description of ENI's commitments and actions on anti-corruption, transparency on payments and organizational transparency.

□ Response by NLNG

In an email dated 17 January 2016, NLNG responded extensively to the findings in our report, by providing a 4-page document. They also refer to their corporate website, www.nigerialng.com, for further information, and indicate their availability to provide further clarifications.

How Shell, Total and Eni benefit from tax breaks in Nigeria's gas industry

The case of Nigeria Liquefied Natural Gas Company (NLNG)

This report presents a case study of Nigeria Liquefied Natural Gas Company (NLNG), Nigeria's largest gas production facility, and examines the way in which its foreign shareholders – Shell (UK/Netherlands), Total (France) and Eni (Italy) – benefit from excessively generous tax breaks provided by the Nigerian government.

The company, NLNG, has been awarded a 10-year tax holiday thanks to an act of parliament created specifically for the venture in Nigeria. This has resulted in the company paying zero taxes for a total period of 12 years: ten years because of the tax break and two further years because of unused tax benefits built up during the 10 years of the tax break. In this report, SOMO has calculated that the total potential lost tax to the Nigerian government amounts to a staggering US\$ 3.3 billion.

SOMO aims to contribute to the discussion on responsible tax governance and financial transparency by presenting factual evidence that tax breaks given to multinational corporations create unacceptable advantages for them that work against the interests of the Nigerian public. The ultimate goal is to raise public awareness of the use and (negative) impacts of tax holidays by multinational companies, using Nigeria as an illustration.

