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Removing Oil Subsidies in Nigeria: Between Necessity and False Economy

Elimma C. Ezeani*

Abstract

The rising costs of oil products on the global market and increasing dependency on fossil fuels have become a concern for both governments and international bodies. Aside from calls to governments to move towards alternatives in the form of renewable energy, the impact of government financial support to businesses in the oil sector in the form of subsides, has also come under criticism. Advocates for oil subsidy removal argue that these subsidies only divert much needed investment in development projects especially in the developing economies, to rich players in the oil sector. In January 2012, the Nigerian government therefore announced its policy to remove the subsidies attached to oil products. The announcement was received with wide public protests which the government sought to calm with a *Subsidy Reinvestment and Empowerment (SURE-P) programme*. This paper considers the broad context of oil subsidy removal in Nigeria. It investigates the necessity behind the Nigerian government's oil subsidy removal policy and evaluates the practical economy of oil subsidy removal in this developing and mono (oil) dependent economy.

Key words: Nigeria, government, oil[1], subsidy, deregulation, necessity, false economy, welfare

1. Introduction: Subsidies in the market economy

Subsidies are a malleable concept; they can be applied towards a variety of purposes from education to healthcare, transportation to consumer goods. Generally, a subsidy refers to support or assistance provided by governments into a sector and paid to a private outfit in order to facilitate the work of the recipient. It is possible to distinguish between subsidies which impact welfare provisions that benefit the poor, and those which directly boost

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[1] In this paper, 'oil' is used in reference to the oil subsidy removal policy in Nigeria. Note however that in Nigeria, 'fuel', 'petrol' and 'oil' are used interchangeably in official documents, amongst members of the public, and in the print media where the oil subsidy policy discussed in this paper has been mainly reported and analysed. The term 'energy' when it is referred to in this paper, is used in its generic sense and in keeping with the intent of any quoted or cited material in this regard.

commercial activity in a specific market. The objective of the latter is to support providers of goods or services in sectors where the government considers that the sector requires such support to enhance its economic contribution. This may be in the form of payments to farmers engaged in agricultural production, such as the often referred Common Agricultural Policy (CAP) of the European Union. On the other hand, welfare subsidies can be in the form of government grants to schools for providing free or reduced education; payments to health operatives for providing services at reduced rates to patients, free transportation for the elderly, etc. Thus, the direct beneficiaries under a subsidy scheme may differ: for a welfare subsidy it may be private individuals and the poor in particular. For commercial subsidies, while the objective still remains the common good, the beneficiaries need not necessarily be determined by their social class, but by whether they consume the good or benefit from the service which has been subsidised. Indeed governments themselves can also gain from subsidies; the prerogative of government initiatives to support or strengthen market activity in a specific sector in a market economy, derives from the understanding that improved commercial activity generates employment, community development and tax profits on the long term, for the government concerned.

In order to appreciate the argument for and against oil subsidies today, it is beneficial to examine the wider notion of subsidies beyond the oil sector and how this issue has been addressed. In the first instance, there is no universal definition on what a subsidy is, and this presents its own challenges. Academic and general definitions variously suggest that a subsidy is "payment by a government to a firm or household that provides or consumes a commodity"[2]; "[A]ssistance; aid in money"[3]; "a sum of money granted by the state or a public body to help an industry or business keep the price of a commodity or service low"[4]; and under the World Trade Organisation (WTO) *Agreement on Subsidies and Countervailing Measures (SCM Agreement,* a subsidy is a financial contribution by a government or a form

[2] Paul Samuleson and William Nordhaus, *Economics* p.982, in Lester n 18 below, 348.

[3] Osborn's Concise Law Dictionary Sweet and Maxwell 11th ed, p398. The term subsidy has its roots in the Latin *subsidium*, meaning assistance.

[4] Oxford Dictionary, Oxford University Press 2013 [Online] available at http://www.oxforddictionaries.com/definition/english/subsidy accessed 2 December 2013.

of income or price support (which increases exports) and which confers a benefit to a specific enterprise.[5]

Incidentally, a subsidy may not and often does not go by the term, 'subsidy'.[6] The problem is further complicated when one attempts to assess whether a payment to a firm or business is a subsidy or not[7] since a subsidy can be direct such as cash payments or grants or indirect, such as in the form of tax breaks or tax concessions.[8] Similar questions have occupied the Dispute Settlement Body (DSB) of the WTO in interpreting whether a government's action amounts to a subsidy and whether that subsidy is prohibited under the aforementioned Agreement (SCM).[9] We can briefly consider the guidance offered from decisions of the WTO. In *Canada – Certain Measures affecting the Automotive Industry,*[10] the Appellate Body held that an import duty exemption granted to certain domestic manufacturers amounted to a subsidy in the meaning of the WTO SCM Agreement since the duty was government revenue which was "foregone."[11] In another case, *Canada – Measures Affecting the Export of Civilian Aircraft*[12] the Appellate body confirmed that to amount to a subsidy, the financial contribution must be by government of which the cost to the government is immaterial, and must confer a benefit or advantage on the recipient.[13]

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[5] Art 1 pursuant to Art XVI GATT, World Trade Organisation (WTO) *Agreement on Subsidies and Countervailing Measures (SCM Agreement).*

[6] See Ronald Steenblik, "A Subsidy Primer" Global Initiative of the International Institute for Sustainable Development , Geneva available online http://www.iisd.org/gsi/subsidy-primer accessed 24 January 2013;

[7] See Alan O. Sykes, "The Economics of WTO Rules on Subsidies and Countervailing Measures" *Olin Law & Economics Working Paper No 186* (May 2003) *(2D Series)* available at http://www.law.uchicago.edu/Lawecon/index.html accessed 24 January 2013 at pp2-5; "The Questionable Case for Subsidies Regulations: A Comparative Perspective" *Stanford Law and Economics Olin Working Paper* No 380 (August 2009)available online: http://ssrn.com/abstract=1444605 or http://dx.doi.org/10.2139/ssrn.1444605 accessed 24 January 2013.

[8] See generally, Global Studies Initiatives, Subsidy Primer – Subsidy Types, International Institute for Sustainable Development, available online http://www.iisd.org/gsi/subsidy-types accessed 23 December 2013.

[9] See generally, Cindy Gallway Buys, "Subsidies and Countervailing Duties" in Carr, Alam, and Bhuiyan (eds) International Trade Law and the WTO The Federation Press 2013, 207-225.

[10] *Appellate Body Report WT/DS139/AB/R and WT/DS142/AB/R 31 May 2000* .

[11] Ibid, para 3

[12] Appellate Body Report, WT/DS70/AB/R 2 Aug 1999.

[13] Ibid para 154 – 157.

Be that as it may, the free market structure if it is to enable businesses flourish, favours subsidies. However the impact of subsidies granted by governments to independent enterprises has always been criticised. Writing in 1979 in the early stages of a shift towards government support for greater commercial activity by private enterprises with the onset of domestic policies on deregulation and privatisation, Nader and Jacobs, commenting on the challenges to US Federal assistance for Chrysler Corporation by General Motors Chairman Thomas Murphy, noted the increasing race by state governments in the USA for the period, towards ever increasing corporate subsidies. They stated:

> Faced with an uncertain national economic outlook, states, cities and towns are competing to obtain a larger share of the country's industry and jobs by offering a growing variety of "incentives" – more accurately called subsidies – to lure new businesses and to encourage expansion of local firms. Prospective employers are offered elaborate packages which can include assistance in site selection, free land, sewerage, even a highway of rail spur, a tax abatement, low-interest loans or tax-free financing, and aid in training new employees.[14]

Concluding their review of US states' practices in granting subsidies in the form of tax-free financing and tax abatements, both considered that "not only do such handouts debilitate the economy, they also, by their backdoor financing technique, escape public accountability and review."[15] In comparison, at the same period i.e. 1979, the UK saw a sudden phasing out of the subsidies to British manufacturing and industrial firms, under the Thatcher-led Conservative government, leading to one of the worst social upheavals in UK history. The objective and impact of this removal of subsides that had kept the manufacturing sector is captured in the statement below:

> The 1979-81 recession was a structural one for manufacturing, and had a brutal purgative effect. When recession began in earnest in April 1980, announced by a collapse in car sales, industry responded like a set of skittles. Only government subsidy kept British Steel, British Leyland and ICL in existence: hundreds of factories closed. In August 1980, 20,000 redundancies a week were being announced - all in manufacturing.

[14] Ralph Nader and Jerry Jacobs "The Subsidy Snowball" The Nation The Nation Company LP, 6 October 1979, 305 – 308 at 305.

[15] Ibid, 308.

> The cruel truth was that many of the companies that went out of business, and many of the managers who lost their jobs, got their just deserts. British industry was overmanned and in large part poorly managed.[16]

The above early observations on the impact of subsidies in sustaining unprofitable businesses, suggest that while subsidies may have helped to prop up businesses and facilitate technical efficiency, they however did not in themselves, make for a stronger or more sustainable industry. These observations appear to persist today. One of the most contested aspects of government subsidy is subsidy to agricultural farmers in Europe and North America. Kumbhakar and Lien in a review of studies on the impact of agricultural subsidies across Europe followed up with empirical research carried out on Norwegian grain farms concluded that while they improved technical efficiency, "subsidies affected farm productivity negatively."[17] Such observations further suggest that subsides possess a moral character: they are either good or bad. Subsidies are good when they do not hamper economic growth and development and are not a burden on resources, but they are bad if they do and ought to be removed. Lester suggests that "one of the fundamental issues with international subsidies regulation is trying to distinguish between 'good' and 'bad' subsidies."[18] He notes that:

> The issue of subsidies is a delicate and complex one. It is delicate in that subsidies are introduced by governments for reasons which they consider to be valid such as the economic development role...Over time, subsidies which once may have served a useful social purpose may have become entrenched and now serve primarily the

[16] David Bowen, "Make or Break: British manufacturing began the eighties with an inevitable shake-out" The Independent , 13 June 1993 available online at http://www.independent.co.uk/news/business/make-or-break-british-manufacturing-began-the-eighties-with-an-inevitable-shakeout-it-started-the-nineties-leaner-fitter--yet-fighting-to-survive-another-downturn-less-shattering-but-harder-to-throw-off-david-bowen-tells-a-tale-of-two-recessions-1491464.html visited 23 December 2013.

[17] Subal C Kumbhakar and Gudbrand Lien, "The Impact of Subsidies on Farm Productivity and Efficiency" in V Eldon Ball, Roberto Fanfani and Luciano Gutinez (eds) The Economic Impact of Public Support to Agriculture – An International Perspective" Springer Studies in Productivity and Efficiency Vol 7 (2010) 109-124 at 122 .

[18] See Simon Lester, "The Problem of Subsides as a means of protectionism: Lessons from the WTO *EC-Aircraft case" Melbourne Journal of International Law* Vol 12 No 2, pp345-372 at 347 .

interests of participants in the industry receiving the subsidies. Eliminating these, then, becomes a local political issue with, perhaps international implications.[19]

In the earlier reference to the 1979 commentary by Nader and Jacobs, the firms which had their activities subsidised were 'for profit' firms. It may therefore have been easier then and now, to criticise government policies that provide businesses which are already making profit with further monies in the form of subsidies. However, the same cannot be said when a subsidy is introduced in an industry that caters for the well-being of people or one that has a welfare objective such as agriculture for example. We can consider "food aid," a practice familiar to the congruence between the free market and development initiatives. Writing on this phenomenon in the context of the World Trade Organisation (WTO) Agreement on Agriculture and what ought to be prohibited subsidies, Kneteman notes that most food aid "is donated or sold on concessional terms to governments and NGOs, who are allowed – or even required – to 'monetise' the donation by distributing the food through local sales at concessional prices'.[20] The end objective in such situations is that the proceeds of the sales are in turn invested in development projects.[21] Kneteman's argument however shows that such subsidies despite their welfare objective was still deserving of criticism since "tied aid" or "in-kind" international food aid was actually a form of export subsidy not protected by the WTO Agreement on Agriculture, and amounted to prohibited and actionable subsidies under the *WTO SCM*. [22]

There is as yet no regulation prohibiting oil subsidies or making them actionable but there has been a lot of criticism and pressure on governments to remove these subsidies. In January 2012, the Nigerian government therefore announced an increase in pump price of petroleum products from ₦65 to ₦140 with immediate effect, following a removal of the subsidies attached to oil products. When the Nigerian government announced the subsidy removal it met with huge protests and much negative publicity. However what was missing from the criticism of the policy, was a review of the wider factors impacting the Nigerian consumer of

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[19] William E. Schrank, "Introducing Fisheries Subsides " UN Food and Agricultural Organisation(FAO) 2008 at pp1-10 at 1.

[20] Christie Kneteman, "Tied Food Aid: export subsidy in the guise of charity" Third World Quarterly, Vol 30 No 6 2009, pp1215 – 1225, at 1216.

[21] Ibid.

[22] See generally Knetman, ibid.

oil products who was affected by the resulting hike in fuel prices at a period of economic hardship not only in Nigeria, but the world over. The nationwide protests were social reactions against the badly timed and poorly advertised hike in petrol prices. The protests worked to a certain extent: the government reduced the benchmark price first proposed and mollified the people with proposed social welfare projects financed under its SURE-P programme which it had based on a forecast of at least ₦ 1.134 trillion per year based on average crude oil price at $90 per barrel into the economy with the subsidy removal. [23] Perhaps what is immediately significant about the oil subsidy removal policy in Nigeria is what it reveals of the challenges to developing strong effective policies in the oil sector. Barely a month after the subsidy reinvestment programme was announced the President recalled the first issue of the SURE document. According to media reports, he stated that the programme had been 'hurriedly conceptualised,' unrealistic, and not feasible.[24] The reason was not for the lack of vision in the programme, but that following the nationwide protests when the subsidy removal had been announced the subsidy removal was not total but only partial and so the projected ₦ I.134 trillion to be recovered yearly from the subsidy removal programme was not guaranteed.[25] The programme was subsequently reinstated but it remains premature to conclude without substantive guarantees by the government in its subsidy reinvestment policies and evidence in the SURE-P programme of action, that the oil subsidy removal will provide much needed stimulation to the Nigerian economy and its efforts at improved welfare for its citizens, or that the country's huge expenditure on supporting a mono-economy can be redirected towards expanding and diversifying the country's economy.

This paper reviews the Nigerian oil subsidy removal policy of 2012 in the wider context of the criticisms against oil subsidies. The paper is in six sections: section 1 introduces the issue of subsides and their impact in the domestic economy and section 2 briefly considers the oil subsidy debate in general. Section 3 examines the arguments on the removal of oil subsidies while section 4 investigates the oil subsidy removal programme announced by the Nigerian government and analyses the rationales behind the subsidy removal. In section 5, the false

[23] Federal Government of Nigeria, *SURE-P Document*, January 2012, 1.

[24] Olusola Fabiyi, 'Fuel subsidy palliatives not possible again' The Punch Newspapers 21 February 2012. Available online at: http://www.punchng.com/news/fuel-subsidy-palliatives-not-possible-again-jonathan/ visited 13 March 2013.

[25] Ibid.

economy of oil subsidy removal i.e. removal of oil subsidies without an adjacent implementation of much needed broader reforms is discussed. The paper concludes in its section 6 by reflecting on the challenges brought forward by oil subsidy removal policies which suggest a necessity for development policy making and a more efficient allocation of government funds but may prove to be false economy in practical terms.

2. The Oil Subsidy debate

The focus on oil subsidies or rather on the need for their removal has been tied to the burden subsidy payments make on governments. This, in our view is perhaps the singular most important factor determining whether a government should or should not remove oil subsidies. Dansie and others state that:

> ..subsidies are a burden on government budgets, especially with high prices for energy on world markets. Although oil prices have been volatile for the last four years, the past decade has shown rising trend, and the prices of other energy carriers are correlated with the oil price. The global recession starting in late 2008 brought about somewhat lower oil prices, but it has actually worsened the burden for subsidising states, as falling tax revenues make it even harder to sustain subsidy levels. This is a significant problem in many developing countries, as increased relative spending on subsidies detracts from other priorities, including education, healthcare and infrastructure. There is also the issue of rent-seeking behaviour: subsidy regimes can encourage policymakers to manipulate subsidy rules for individual rather than collective gain.[26]

The authors of the above argue further that subsidies: defeat the objective of energy conservation which cannot be met for as long as prices remain low; lead to higher energy

[26] Grant Dansie, Marc Lanteigne, Indira Overlord, "Reducing Energy Subsidies in China, India and Russia: Dilemmas for Decisin Makers" *Sustainability* 2010, 2, 475-493 at 477. The authors acknowledge that governments justify their subsidy grants for two reasons: to promote economic development and to benefit the poor – see p477 but consider that these benefits are only for the short-term. For other critical reviews of oil subsidies ; Anja Von Moltke, Colin Mckee, Trevor Morgan, Energy Subsidies: Lessons Learned in Assessing their Impact and Designing UNEP, Greenleaf Publishing 2004.

consumption with a resulting impact on the environment; are a barrier to development of renewable energy and subsequently cause severe environmental problems; and result in poorer investment decisions on capital equipment and infrastructure in the energy sector. [27] Their enquiry into the "dilemma" facing decision makers in removing oil subsides revealed that in the three countries studied – China, Russia and India, the decision makers have approached the task with caution; indeed it could be said that caution is a necessity for the success of the policy itself.

Other writers have assessed the necessity of removing energy subsidies often in favour but with directions on how governments and policy makers are to manage the process. Reviewing Ghana's oil subsidy removal programme in 2011/12, Crawford argues that policy makers must communicate planned removals efficiently especially in view of those with "powerful interests" and for the understanding of the general public.[28] Others advocate that mitigating the financial impact on the public (referring to experiences in Mozambique, Jordan and Indonesia), promoting transparency in petroleum subsidy accounts, and timely information to the public, are integral to a successful oil subsidy removal programme.[29] Assessing the impact and design of energy subsidy policies, Moltke and others argue that the financial value of energy subsidies generally speaking, are of minor significance to poor households and that where rationing results as a result of a cap in prices it is rich families that will be able to access these products as a result of "petty corruption and favouritism." [30] They therefore conclude that governments should "actively involve stakeholders in the process of formulating policy."[31] However Moltke and others appear to hesitate at their own suggestion; in the same passage, the authors acknowledge the difficulty policy makers face and the need for a strong political will to introduce such removal programmes. They suggest further, that any changes must be accompanied by visible efforts to ameliorate the impact on the public.[32]

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[27] Ibid.

[28] See generally, Guy Crawford, "Ghana's Fossil-Fuel Subsidy Reform", IDS (2009).

[29] David Coady et al, "Petroleum Products Subsidies: Costly, Inequitable, and Rising" *IMF Staff Position Note* SPN/10/05 Feb 25 2010 at 14-5.

[30] Anja Von Moltke, Colin Mckee, Trevor Morgan, Energy Subsidies: Lessons Learned in Assessing their Impact and Designing UNEP, Greenleaf Publishing 2004, at 144.

[31] Ibid, 146.

[32] Ibid.

Arguments in favour or against oil subsidies have however mainly been at a macro-business level and have focused on how much subsidies cost the poorer members of society to the benefit of the rich. According to the International Energy Agency (IEA), subsidies applied to fossil fuels do not benefit the poor, distort the market, and are an inefficient allocation of resources.[33] The IEA calculates that subsidies paid out in 2010 totalled $409 billion and contrary to national projections that subsidies alleviate poverty and promote economic development, they have "unintended consequences".[34] By contrast, the American Petroleum Institute (API), resisting the attempts by US President Obama to end subsidies (tax breaks) to oil firms in 2011-12 proffered the arguments below:

> The oil and natural gas industry is one of the world's largest and most capital-intensive industries. It has to be to effectively compete for global energy resources. The industry's earnings make possible the huge investments necessary to help ensure America's energy security. The earnings allow companies to reinvest in the facilities, infrastructure and new technologies that keep America going strong well into the future while generating returns that meet shareholder expectations....
>
> Contrary to popular belief, and what some politicians might say, America's companies aren't owned just by a small group of insiders. Only 2.8 percent of industry shares are owned by corporate management. The rest is owned by tens of millions of Americans, many of them middle class.
>
> Some policy makers have been using profit numbers from the five largest oil and natural gas companies operating in the U.S. to make the case for higher taxes. This is, at best, an incomplete picture. While they point out that between 2006 and 2010 these five companies had a net income of $484 billion, what they don't tell you is that during that same period the five companies' profit margin was 6.65 percent. What they also don't tell you is during that same period these companies incurred $377 billion in income taxes – putting their effective tax rate at 43.79 percent.[35]

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[33] IEA/OECD, "World Energy Outlook – IEZ analysis of fossil-fuel subsidies" Paris, 4 October 2011 available online: http://www.iea.org/publications/worldenergyoutlook/resources/energysubsidies/ accessed 25 January 2013.

[34] Ibid.

[35] See the American Petroleum Institute (API) "Putting Earnings into Perspective: Facts for addressing energy policy" pp 1, 2, 9.

These two diverging views which reflect the general arguments for and against in debates on subsidies in this sector from the IEA and the API, do have something in common: they are primarily concerned with the very big picture: subsidies in the upstream sector i.e. subsidies granted to businesses engaged in oil exploration and production or with subsidy payments that end up with businesses in the oil sector. What happens at the policy level when governments, in particular developing country governments where the energy sector in itself is grossly inefficient and where high consumer prices are further compounded with constant scarcity, adulteration, unregulated black market activity, and low living standards are faced with oil subsidy removal? Does the policy of removal respond to the parallel consumer demands for oil products in addition to meeting the forecasted benefits to the government post subsidy removal? What about the policy of subsidy removal and the impact on lives and businesses who not only have to purchase oil products at higher costs, but who also have to bear with the ever increasing costs of living and welfare?

3. Removing Oil subsidies

A 2006 World Bank study on phasing out subsidies notes the following:

> To provide a subsidy, a government must increase its borrowing, raise additional revenue elsewhere, or reduce spending on other public goods. If the subsidy is used to stabilise or lower final prices, it frees consumers from having to adjust their purchasing behaviour to the costs of supply, instead giving them financial incentives to overconsume the subsidised commodity. The result is the well-known deadweight loss.[36]

In the broader context of energy subsidy removal, at international level the concern is that states ought to address inefficient subsidies.[37] Where subsidies are effectively managed, they can facilitate wealth distribution and encourage growth in underperforming sectors. Given the various interests both in their allocation and application, problems can therefore arise in their

[36] Robert Bacon and Masami Kojima, "Phasing out Subsidies – Recent Experiences with fuel in developing countries" The World Bank Group August 2006 p2; cf J.Atsu Amegahie, "The Economics of Subsidies" Crossroads Vol 6 N 2, pp7-15.

[37] See the OECD, "Inventory of estimated budgetary support and tax expenditures for fossil fuels (2011) . the inventory is of OECD Member countries.

implementation and management which may lead to the aforesaid inefficiencies. We consider that such inefficiencies can include: determining the sector in which to apply subsidies, how much is to be paid; the source of funding, keeping records of subsidies paid, to whom and for what period; inspection checks; averting fraud; addressing potential loss or reduced activity in unsubsidised sectors; strain on social services with migration shifts to better paying industries; the possible decline of market activity for unsupported sectors; addressing multilateral concerns that subsidy payments encourage protectionism; evaluating the efficacy of subsidies. In our view, the greater difficulty however arises where countries decide to remove subsidies under a government reform policy without a strong framework for implementing the reforms. In a World Bank case study of twenty developing countries by Vagliasindi, she noted lessons from "poorly implemented subsidy reforms" as follows:

> Universal energy-price subsidies tend to be regressive as benefits are conditional upon the purchase of subsidized goods, and increase with expenditure. The proportional adverse impact of energy subsidy removal can be greatest for the poor, even though the rich receive most of the value of the subsidy (IEA, OPEC, OECD, World Bank, 2010).[38]

A significant finding of Vaglisandi's case study is that:

> An important condition for successful reforms is the credibility of the government commitment to compensate vulnerable groups and to use the funds freed from subsidy reform for more welfare enhancing activities. Policy tools to protect the poor include and lifeline rates, which generally perform better than universal subsidies as well as cash transfers. Use of transitional arrangements and short term measures to alleviate the impact of tariff increases on the poor can act to protect low-income groups at the time of the policy change.[39]
>
> ...Governments need to ensure public trust in the reform agenda through broad communication, appropriate timing of subsidy removal, and implementation of compensatory social policies. Explaining the need for change and the compensating measures that will be undertaken, before the changes are introduced, reduces

[38] See Maria Vagliasindi, "Implementing Energy Subsidy Reforms: An Overview of Key Issues" Policy Research Working Paper 6122, The World Bank, July 2012.p2.

[39] Ibid, p22.

uncertainty and can make the case for reform stronger. Planning careful communication strategies including media and public campaigns in order to reach out to the poor and those who will be most affected by the subsidy reform can help minimize public opposition to energy subsidy reforms.[40]

It is interesting to note further that the case study also emphasises the value of "ensuring the sustainability of subsidy policy through broader sectoral reforms."[41] In Nigeria's case, such broader sectoral reforms would include guaranteeing the availability of oil products to consumers across the country, improving the efficiency of marketing, transportation and distribution networks of oil products across the country, ensuring the quality and safety of oil products available to the public, guaranteeing a uniform price for oil products available at fuel stations across the country, and improving road infrastructure and road networks including efficient public transport for those persons who cannot afford the higher prices that are ushered in with oil subsidy removal.

4. The Nigerian Oil Subsidy Removal Programme

In Nigeria, the issue of oil subsidy removal had earlier been raised under the Structural Adjustment Programme (SAP) liberalisation agenda in the 1980s. It ignited debates and strike action in 1986, and again in 1993 under respective military governments. [42] The oil subsidy removal agenda which forms the basis of this paper's enquiry was set out in Nigeria's Subsidy Reinvestment and Empowerment (SURE-P) Programme.[43] The agenda makes a strong case for discontinuing fuel subsidies because "this poses a huge financial burden on government, disproportionately benefits the wealthy, is inefficient and diverts resources away from potential investments in critical infrastructure."[44] The discontinuation is expected to

[40] Ibid, p27.

[41] Ibid, p29

[42] See Peter Esele, 'Removal of Subsidy: Hard Road to Travel, This Day Nigeria 24 October 2011, p80; See Adedoyin Ogunade, 'Oil Subsidy and the economy' *The Guardian Nigeria* , 17 March 1993, p29; Toye Akinrinole and Tunji Oyewo, 'Why subsidy on aviation fuel was removed - Olashore' *Nigerian Tribune* 19 March 1993 p2.

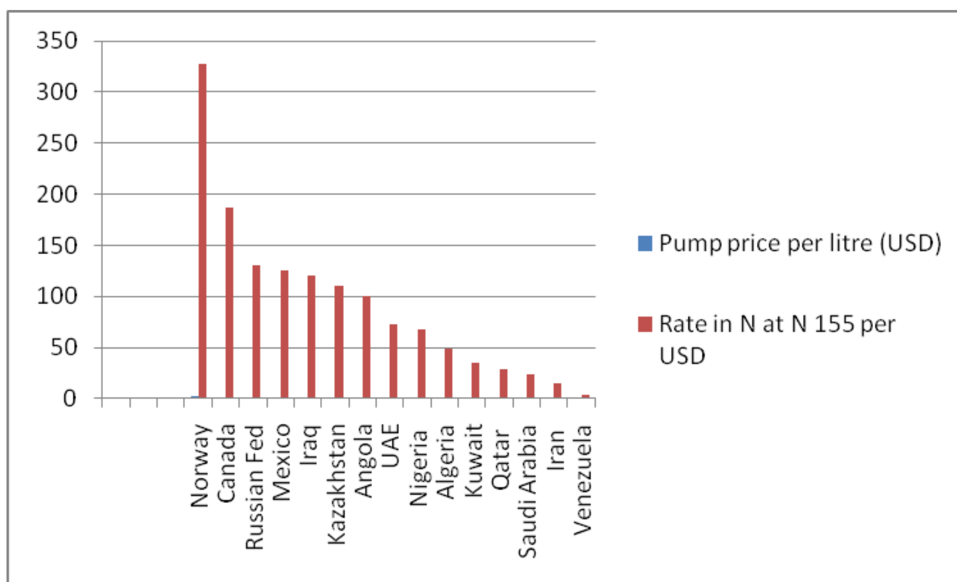
[43]Federal Government of Nigeria, *SURE-P Document*, January 2012.

[44] Ibid Para 2

"save additional resources for investing in programmes targeted at mitigating poverty and spurring economic growth."[45] This is the crux of the issue – that the subsidy removal programme can and will stimulate economic and social advancement in Nigeria.

Some critics of the programme immediately questioned the benefits to the poorest fuel consumers. A ground for this criticism was that the Nigerian consumer had even before the subsidy removal, paid the highest pump price compared to their counterparts in other oil exporting nations.[46] This ground however does not hold up to scrutiny if one compares the pump prices of the top fifteen oil exporting countries in USD as we have done in the figure below:

Figure 1: Comparison Tables – Top Oil Exporting countries and in-country Consumer Prices for 2008-2012 (For table of data, see Appendix A)



Source: compiled from figures from World Bank data on top oil exporting countries and consumer prices (Ezeani, 2013)[47]

[45] Ibid, Para 10.

[46] See for instance, Mercy Odeh Adiza, "Deregulation Policy in the Downstream Oil Sector and the Nigerian Economy" *Journal of Science and Public Policy* Vol 3 Dec 2011 Cenresin Publications pp83-100 at 96-7; Okey H. Ovaga "Deregulation of Downstream Oil Sector in Nigeria: Its Prospect" *Journal of Science and Public Policy* Vol 2, Dec 2010 Cenresin Publications pp115-129 at 124-5.

[47] Pump Price data is extracted from World Bank: "Pump price for most widely sold gasoline – US $ per litre", available at http://data.worldbank.org/indicator/EP.PMP.SGAS.CD/countries?display=default accessed 28

From the above, Norway which has one of the highest GDPs in the developed world had the highest pump price rate for the period 2008-2012. The next two highest pump price countries were Canada and Russia; the pump prices were even given the relatively wealthy economies of these countries, still significantly high for consumers.[48] For Russia in particular which has kept gas prices low over the years with the contribution of subsidies to the sector, attempts to remove these subsidies have been met with social discontent;[49] and despite the subsidy, the costs to the consumer are still higher than that to the Nigerian consumer's pump prices. There are still other countries with very high standards of wage earning per person, but very low consumer costs for e.g. Qatar, the UAE, and Saudi Arabia. Yet consumers in other states like Venezuela with a relatively low per capita income per household offer gasoline at very low prices as the table above reflects. Thus while it is fair to say that the Nigerian consumer pays a high price for petroleum products, that cost is not the highest across oil exporting countries.

On the other hand, the government offered up a number of reasons for the oil-subsidy removal. These included: that oil subsidies benefitted only the rich to the disadvantage of the poor; that the oil subsidy removal represents an effort to rebalance the costs and benefits of oil consumption to the advantage of the poor; that the oil subsidy was responsible for smuggling and fraud in the oil sector; that the oil subsidy was responsible for inaction with regard to the construction of refineries in spite of licences issues to the private sector; that removing oil subsidies is a deregulation policy; and that oil subsidy removal guarantees affordable consumer prices for oil products.[50] We investigate these rationales below.

4.1 The oil subsidies benefitted only the rich to the disadvantage of the poor

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January 2013. Note that rate in Naira does not reflect decimal prices. Also, country list is not in order of production capacity but in descending order of pump prices.

[48] Ibid.

[49] See generally, Indira Overland and Hilde Kutschera, "Pricing Pain: Social Discontent and Political Willpower in Russia's Gas Sector" Europe-Asia Studies Vol 63, no 2 March 2011 pp311-331.

[50] See generally, Ngozi Okonjo Iweala (Coordinating Minister for the Economy/Honourable Minister of Finance, Nigeria): *"Brief on Fuel Subsidy"* Federal Ministry of Finance, Nigeria 6 December 2011

The most widely communicated proposition for the oil subsidy removal by the Nigerian government was that energy subsidies "benefit mostly the rich"[51] and that the subsidy "does not reach intended beneficiaries." The first argument is mainly populist; the second is an impractical analysis of those who consume oil products in Nigeria which includes the rich and the poor. It is surely the better view that it is a government's responsibility to identify in its development programmes, those sectors wherein development projects are required and to apply subsidies to that sector. If a government chooses to apply subsidies to a sector which is not favoured by the poor, does not directly impact the living standards of the people, or does not stimulate economic activity, this is a default in the government's development policy and planning schemes, not a blame on the beneficiaries of the subsidies. Second, subsidies may or may not directly impact poverty levels – it depends on the nature of the subsidy and the sector of application.

Oil subsides in Nigeria's case, may not have directly benefitted the poor and this is not just because the poor do not drive cars (a doubtful statement even in Nigeria where with poor public transport infrastructure, a car is more a necessity than a status symbol). The nature of the oil market – a high-income earning product that demands huge capital investment in its operations must be taken into consideration. Access to downstream operations as suggested earlier, is typical to high-income earning firms owned and run by people with the investment capital needed to engage in the downstream sector in the first instance. Subsidies in this regard will obviously benefit the already rich who can engage in this market. This does not mean that the said rich are robbing the poor; it is just that the poor hardly operate businesses in that sector.

Furthermore, insisting that the oil subsidy did not benefit the poor suggests that the Nigerian oil subsidy scheme was for the benefit of the poor in the first instance. Since there is no record of the rationale for subsidy allocations one cannot say for certain that the oil subsidy payments made before 2000 were for the purposes of poverty alleviation and economic developments as is alleged. The argument for the *removal* of subsidies however, does raise these factors which are actually supply side constraints in Nigeria's domestic market, as the government's primary concerns for removing the oil subsides. It was not surprising therefore that the welfare objectives under the SURE-P programme proposed to address what has been

[51] Ibid, p6

a persisting social deficiency under various Nigerian governments. The projects to be covered included maternal and child health services, public works women and youth employment programmes, urban mass transit scheme, and vocational training schemes. However, this is all the subsidy removal programme does – divert funds from a commercial but unregulated subsidy scheme to an equally unregulated or at best unplanned programme of welfare infrastructure. For this reason, the SURE-P programme and its implementation has attracted a lot of criticism mainly on the absence of any clear details on how the monies gained from the subsidy removal will be applied to welfare projects across the country.[52] Therefore the government's suggestion that subsidy removal frees up funds for welfare projects may have been an appeal to populism, but it is hardly the economic watershed for Nigeria's development it is touted to be and it remains to be seen how the monies recovered from the oil subsidy removal will improve the lives of the poor.

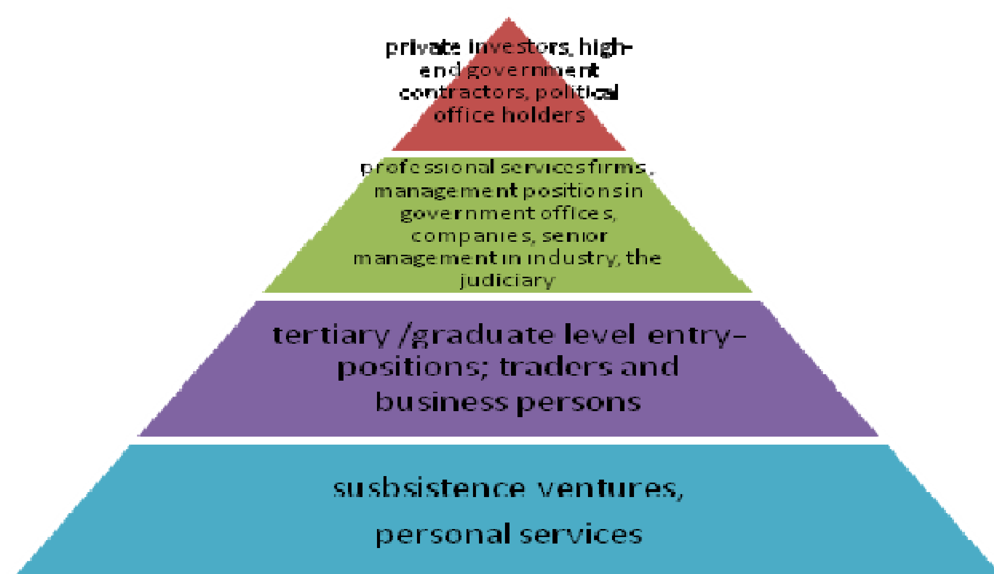
4.2 Oil subsidy removal represents an effort to rebalance the costs and benefits of oil consumption to the advantage of the poor

In Nigeria's case, it is not clear whether the funds saved under the subsidy removal scheme are *an addition* to already existing funds available to the Nigerian government from its national income. This would mean the government has increased funding available not only for socio-economic projects, but also, funding for other projects that can usher in a diversified economy with potentials for competitive advantage. The SURE-P programme does not make any such suggestion although from the government's pronouncement on this second rationale for the oil subsidy removal, one may easily conclude that the subsidy payments were the reasons for the lack of basic infrastructure provision over time in the country which is why the oil subsidy funds will now be applied to social projects. Needless to say, this is not the fact.

[52] See "How Jonathan's Subsidy Reinvestment Programme SURE-P Fumbled at Budget Defence" *Marine and Petroleum Nigeria* Vol 12 (2013) online at: http://www.marineandpetroleum.com/node/44 accessed 8 February 2014; see also House of Representatives Nigeria, "State of the Economy: Observations, Requests for Additional Information and Invitation to Investigative Hearing" *Letter to the Hon Minister of Finance and Coordinating Minister for the Economy* 31 January 2014.Also available online –see Idris Akinbajo, "House Committee rejects Okonjo-Iweala answers to 5o questions, asks her to reanswer" *Premium Times* 3 February 2014 at: http://premiumtimesng.com/news/154470-house-committee-rejects-okonjo-iwealas-answers-to-50-questions-asks-her-to-reanswer.html accessed 8 February 2014.

There is of course a valid argument against fixed, albeit cheaper, fuel [oil] prices which not only distort the market but can prove a barrier to competition.[53] As opposed to government fixing prices of oil products, allowing the Nigerian market to dictate prices may improve the function and efficiency in that market. However, one cannot assume that markets will function in practice as they are expected to in theory, without an enabling environment especially when the majority of businesses are small businesses and the most common form of business association is sole trading, as in Nigeria's case. This is of course not a theoretical argument but a practical one and is better understood when we ask what kind of businesses the rich and poor in Nigeria, both of whom are customers in the oil market are actually engaged in. The pyramid below captures this social and business stratification of the Nigerian oil consumer.

Figure 2: Pyramid showing business strata in Nigeria:



Source: Independent interpretation of share of income and business trends in Nigeria (Ezeani 2013)

All four strata above use oil products in both their private and business lives: for transport (private or public), for business purposes (including fuelling generators) or for use in their

[53] Jean Balouga, 'The Political Economy of Oil Subsidy in Nigeria,', International Association for Energy Economics (Second Quarter 2012) pp31-35 at 32.

private homes again, for powering generators with the constant power outages experienced as a matter of daily living in Nigeria. Just as the rich supposedly benefit from subsidies because of their greater access to capital ventures that operate oil businesses, they are also likely to face fewer difficulties when subsidies are removed and the prices of oil products are higher. Removing oil subsidies on its own is therefore no guarantee that the costs and benefits of oil consumption are rebalanced to the benefit of the poor. As Vaglisiandi noted, broader sectoral reforms are imperative if an oil removal subsidy policy is to be successfully implemented.[54] We will return again to examine these reforms in the Nigerian context, in greater detail in section 5 of this paper.

4.3 The oil subsidy was responsible for smuggling and fraud in the oil sector

The third rationale for removing the fuel subsidy is that this would decrease smuggling activities, and reduce fraud and rent-seeking behaviour in the sector.[55] Again, rather than being an indictment on subsidies, this negative consequence reflects financial mismanagement and corruption by those agencies of government that implement the subsidies. Furthermore, it raises a crucial question of control of Nigeria's borders and the national security imperatives of the Nigerian government. Those who have reported on, or worked within the energy sector in Nigeria, have offered an insight into the somewhat confusing operation of the downstream sector.[56] Without a clearly defined route that sets out the 'subsidy' payments made on the importation, distribution and transportation of petroleum, it is difficult to determine the exact cycle of the oil subsidy scheme. Nevertheless we can suggest what transpires, at least before the proposed subsidy removal, in the cycle represented below:

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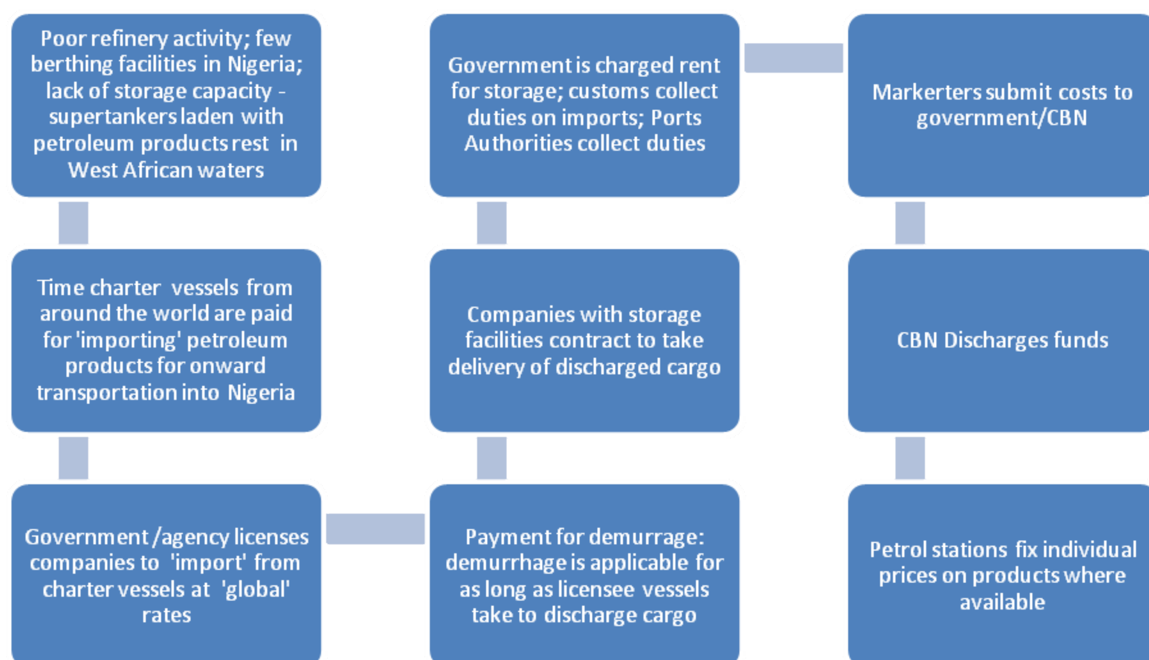
[54] n 38 above, pp29-30.

[55] Ibid.

[56] See Olusegun Adeniyi, "The Subsidy Payments" This Day Newspapers Nigeria, 2 February, 2012. Available online http://www.thisdaylive.com/articles/the-subsidy-payments/108367/ accessed 30 January 2012; Editorial: "Kerosene and the Phantom Subsidy", Nigerian Tribune newspapers 19 July 2011, p 17; Farouk Lawan, "Porosity at the Borders: Who's Culpable?" This Day newspapers, 3 February 2012 p32; Kingsley Omose, "Understanding the fuel subsidy riddle" The Punch newspapers 21 October, 2011, p16; Kehinde Laniyan, "The rich, the poor and fuel subsidy" Saturday Champion, 17 December 2011, p38.

Figure 3: Cycle of Subsidisation of petroleum products Nigeria pre- January 2012:



Source: Interpretation of cycle from government material, newspaper accounts, public commentary (Ezeani 2013)

The many anomalies including supply side constraints which stifle production capacity and trade facilitation in the Nigerian market have not been addressed by the subsidy reinvestment programme. We can extrapolate from the above figure to identify these anomalies. They include:

- Poor government administration of the (domestic fuel) market;
- Lack of accountability by marketers and distributors (in the oil subsidy scheme);
- Unaccounted payments and overspending by the Central Bank (in payments to government contractors);
- Loopholes in an unregulated process;
- Poor border and customs security;
- The potential for 'creative accounting' applied in determining operators' expenditure on freight, storage, ports and other charges;
- Cartelisation;
- Laissez-faire attitude towards operation of both the upstream and downstream operators especially in issues affecting individuals e.g. oil spillage, gas flaring, environmental degradation, human rights abuses etc;
- Absence of adequate evaluation over licensing agreements for the construction of new refineries;
- Absence of the rule of law and of effective government enforcement mechanism to counter market distortion activities; and
- Poorly conceived policies and strategy in subsidy allocation and implementation.

Incidentally, these issues have been highlighted by the government itself when it considered that the subsidy payments rather than meeting the objective of efficient downstream operations, fostered fraud, smuggling and black market activity. While these anomalies have been exposed under the oil subsidy scheme, the oil subsidy removal policy to be effective has yet to address or counter them.

4.4 The oil subsidy was responsible for failure of private sector licensees to build refineries:

The government asserts that of the twenty refinery licences issued to private firms as a measure to tackle the need to import refined oil products and reduce the associated high costs of importation since 2000, none of the licensees had built a refinery.[57] The preference was instead for marketing imported oil products. This excuse for a potential breach of licensing

[57] n50 above, p6.

agreements is a strange admission of incompetence for how does the ‘cycle’ above stop the construction of refineries? The answer is simple: cartelisation - these firms who engage directly with the vessel owners, ports authorities, storage facility owners, transporters, etc are in the absence of government regulation of the downstream sector, able to demand any sums from the government and the Central Bank as their incurred expenditure for the importation and distribution of petroleum products. Considering the loopholes in this unregulated but highly profitable sector, it should be no surprise that the profits of engaging in the ‘market structure’ above far outweigh the costs of constructing new refineries. This problem of cartels aside, there is also concern with the process of awarding licences for constructing refineries. Given the unstable and unregulated structure of the domestic fuel market, surely it ought to have been a prime factor in short-listing potential licensees, that they were competent and capable of constructing the refineries regardless of the distortions in the market? The government could also have pursued the licensees to carry out their obligations and where licensees were engaged in marketing and distribution (and therefore collecting subsidy payments), they could have been identified and their refinery licensees withdrawn or their contracts to market oil products rescinded. However the government was trapped in maintaining the subsidy payments because it had neither an alternative to the market cycle depicted above nor, any means of regulating the activities of the firms operating in that structure. The Central Bank in collaboration with the other agencies that administered the subsidy scheme has by its own admission, paid unaccounted sums to downstream operators.[58]

4.5 Removing oil subsidies amounts to a deregulation of the downstream oil sector:

In order to deregulate i.e. to limit the involvement of government’s regulatory and law-making powers in a sector, there must first be regulation present. This has not been the case strictly speaking, in the country’s oil and gas sector. Various efforts at a *composite* legal regulatory framework that would regulate both upstream and downstream activity in Nigeria had been made without much success since the return to democratic rule – the first in 2004

[58] Henry Boyo, “Exploring sustainable alternative to fuel subsidy removal” The Punch newspapers, 27 January 2012 p64; Sunday Ojeme “FG spent N2.07tn on petroleum subsidy in five years – PPPRA” The Punch 16 Decemebr 2010, p 15; Onwuka Nzeshi and Emele Onu, “Samusi: Petroleum Subsidy gulps N1trillion in 4yrs” This Day newspapers, 18 February 2010 p3; Victor Oluwasegun, “Remove fuel subsidy now, Sanusi advises Federal Govt” The Nation, 8 June 2010 p 2; Editorial, “Fuel Subsidy: Cost of governance” The Guardian Nigeria 26 January 2012, p 14.

when a "Bill for Petroleum Products and other oil related activities compensatory relief bill" was first proposed.[59] At present, a proposed *Petroleum Industry Bill* (PIB)[60] includes amongst its objectives, "to deregulate and liberalise the downstream petroleum sector."[61] This proposal still under consideration by the Nigerian legislature is in real terms, the first definitive effort at providing a regulatory framework for Nigeria's upstream and downstream sector.

Definitive (non-legislative) attempt at regulating the downstream oil sector in Nigeria began with the efforts at addressing the payment of oil subsidies in Nigeria to petroleum marketers variously contracted with the government. This was in 2000 under the Obasanjo Administration. That Administration established the Petroleum Products Pricing Regulatory Committee (PPPRA), an agency which was to amongst other things, "determine the pricing policy of petroleum products, and regulate their supply and distribution".[62] The PPPRA was to "establish and maintain" funds for its duties.[63] There is no mention of 'subsidy payments' from such funds in the Establishing Act of the Agency.[64] However, investigations by the House of Representatives following national strike action when the subsidy removal was announced by the government on 1 January 2012 reveal that the subsidy payments were made from a Petroleum Support Fund (PSF) provided for in the national budget.[65] The House of Representatives report which investigated the subsidy arrangements from 2009 to 2011 (both years inclusive) identifies one hundred and twenty-eight marketers engaged in the subsidy scheme; it also establishes that the fund was managed under guidelines set down in 2006.[66]

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[59] See the various Bills on the Nigerian National Assembly web page: http://www.nassnig.org/nass/legislation2.php?search=petroleum&Submit=Search accessed 24 January 2013.

[60] "A Bill for an Act to provide for the Establishment of a Legal, Fiscal and Regulatory Framework for the Petroleum Industry in Nigeria and for other related matters" (2012). The Petroleum Industry Act 1969 was the first legal framework for petroleum activity in the country. It was focused on the upstream sector and provides for the exclusive authority of the Minister for Petroleum in the award of exploration licences.

[61] Petroleum Industry Bill, op cit, S1(f).

[62] Federal Government of Nigeria (FGN): *Petroleum Products Pricing Regulatory Agency Bill* Part 2 Functions and Powers of the Agency, S.7 (27 May 2003). See generally S7(a-m).

[63] Ibid, S.10(a-e).

[64] n 62 above.

[65] See the National Assembly, Federal Government of Nigeria (FGN): "Report of the Ad-Hoc Committee to verify and determine the actual subsidy requirements and monitor the implementation of the subsidy regime in Nigeria" *Resolution No(HR.1/2012)* 18 April 2012, Chapter 4.

[66] Ibid.

Given the remit of that report, regulation of market activity under the subsidy scheme prior to 2009 is not examined.

From the PPPRA historical time line of activities,[67] the Agency sets the start of a 'regulated regime' as 14 August 2000, the date when a Special Committee on the Review of Petroleum Products Supply and Distribution (SRCPPSD) was set up.[68] Between 14 August 2000 and 29 September 2003 when the supposed 'deregulation regime' was implemented,[69] the only significant events relevant to regulation and deregulation properly so called are the establishment of the PPPRA in March 28 2001, and the signing of the PPPRA Bill into law by the President, on May 27 2003. The other events carried out by the agency were procedural including opening up the Apapa Lagos jetty for all users on a fee basis on 29 September 2003, training programmes for the Agency's staff, preparation of documentation templates for importation activities, meetings with the Central Bank of Nigeria (CBN) mostly related to release of foreign exchange (Forex) for marketers, and various meetings with 'stakeholders' across the country.[70] Therefore, the notion that the subsidy regime in the petroleum sector was 'regulated' from 2000 and thus that the establishment of the PSF in 2006 was a deregulation mechanism, is questionable. What began in 2000 was the initiation of a discernible market structure to streamline divergent processes for the marketing and distribution of petroleum (involving the CBN, the Accountant-General of the Federation, the Honourable Minister for Petroleum, Ports and Customs Authorities, other government personnel) and to attach responsibility for financial disbursements for these activities to a definite agency, the PPPRA.

The legality of the government's effort at deregulation by its oil subsidy removal policy has also been the subject of judicial review. In *Bamidele Aturu v Minister of Petroleum Resources and the Attorney General of the Federation*[71] the plaintiffs sought a declaration that the deregulation policy of the government and the government's decision not to fix prices

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[67] See the PPPRA web page: *Major Historical decisions* - http://www.pppra-nigeria.org/decisions.asp accessed 24 January 2012.

[68] Ibid.

[69] Ibid.

[70] Ibid.

[71] FHC/ABJ/CS/591/2009; judgment delivered, 19 March 2013.

of petroleum products were in contravention of S6 of the *Petroleum Act 2004* and S4 of the *Price Control Act 2004.* They also asked the Court to declare that such action by the government was contrary to the government's obligations under S16 (1)(b) of the Nigerian Constitution to "secure maximum welfare, freedom and happiness of every citizen" and made the guarantee of freedom of movement under S41, "illusory." In its opinion, the court upheld the motion by the plaintiffs holding that the "deregulation policy" was "unconstitutional, illegal, null, and void."[72] The Court therefore ordered the government to publish the prices of petroleum products regularly for the benefit of the public.

In fact, 'regulation' of the Nigerian petroleum sector is a nascent exercise and the subsidy removal programme of January 2012 cannot properly be referred to as a 'deregulatory' effort. It is at best an attempt at restructuring and hopefully creating a liberal market structure in the country's petroleum sector. More importantly, it addresses corruption and mismanagement of national funds in the sector. Fuel including petrol, diesel and kerosene have always been sold at lower rates than global prices in Nigeria (and therefore effectively subsidised in some form) prior to 2006 when the PSF guidelines on subsidy payments were established.

The above facts often missing from the debates on fuel subsidy and its development impact in countries like Nigeria further distort the arguments for and against removal of oil subsidies as an efficient deregulatory measure.

4.6 Oil subsidy removal will guarantee affordable consumer prices

In the absence of any regulatory mechanism, pump prices of petroleum products were arbitrarily fixed by government or at least, fixed according to government's unexplained estimates. The table below sets out the prices of fuel between 1977 and 2009.

[72] Ibid.

Figure 4: Price fluctuation of premium motor spirit from 1977-2009 (price L^{-1})

Year	Price L^{-1}	Fluctuation	Increase (%)	Decrease (%)
1977	3K	-		
1978	8.5K	Increase	183.33	
1979	13.5K	Increase	58.82	
1980	15K	Increase	11.11	
1981	15K	Increase	0.00	
1982	20K	Increase	33.33	
1983	30K	Increase	50.00	
1984	30K	Increase	0.00	
1985	39 ½ K	Stable	31.67	
1986	39 ½ K	Increase	0.00	
1987	42K/60K	Stable	6.33/51.89	
1988	60K	Incre/stable	42.86/0.00	
1989	60K	Increase	0.00	
1990	70K	Stable	16.67	
1991	70K	Increase	0.00	
1992	#5.00	Stable	614.29	
1993	#3.25	Decrease		35.00
1994	#11.00	Increase	238.46	
1995	#11.00	Stable	0.00	
1996	#11.00	Stable	0.00	
1997	#15.00	Increase	36.36	
1998	#15.00	Stable	0.00	
1999	#20.00	Increase	33.33	
2000	#22.00	Increase	10.00	
2001	#26.00	Increase	18.18	
2002	#30.00	Increase	15.39	
2003	#40.00	Increase	33.33	
2004	#49.00	Increase	22.50	
2005	#52.00	Increase	6.12	
2006	#64.50	Increase	24.04	
2007	#75.00	Increase	16.28	
2008	#75.00	Stable	0.00	
2009	#65.00	Decrease		13.33

Source: Ogunbodede, Ilesanmi and Olurankinse (2010) [73]

The figures above are 'official' figures only i.e. the prices government announced as pump prices. The situation in real terms was very different. Fuel was more commonly scarce and if available, at significantly exorbitant prices fixed by the pump station owners themselves. Long queues at petrol stations and black market activity were the norm especially between

[73] E.F. Ogunbodede, A.O. Ilesanmi, F.Olurankinse, "Petroleum Motor Spirit (PMS) Pricing Crisis and the Nigerian Public Passenger Transport System" *The Social Sciences,* Vol 5 Iss 2 Medwell Journals (2010) pp113-121, at 114.

1986 and 2009; between 1992 and 1994, the crisis was at its worst and that period recorded one of the most protracted national strikes by labour unions in Nigeria with attendant social upheaval in the country.

The queuing situation may have improved with the current adjustment that raised the official pump price of petrol from ₦ 65 per litre[74] to ₦ 136 after the subsidy removal was announced, and then the current official price of ₦ 97 following national protests. It may be that this latter price more closely reflects the costs of transportation and 'unofficial facilitation payments borne by marketers in the course of distribution. However, as at the first quarter of 2013, fuel was typically sold at ₦ 110-120 regardless of this official price.

Without considering and factoring in the broader reforms that can facilitate the objectives of oil subsidy removal and without taking into account the local circumstances of the country, oil subsidy removal programmes may end up costing governments more than they may have forecasted and prove to be false economy.

5. The False Economy of Oil Subsidy Removal

It is important to explain what we mean here by false economy. Here we refer to the error in expecting that a particular action that reduces government spending in one sector, will invariably yield a benefit to the wider economy. We had earlier referred to Vaglisani's criteria for ensuring the sustainability of subsidy policy and her views also inform our discussions in this section.

On the best approach to designing subsidy policies in the energy sector in general, Moltke and others note that:

> There is no single right approach or model to designing or reforming subsidy policies. Every country needs to take account of national and local circumstances. These include the country's own policy objectives and priorities, its stage of economic

[74] See Okonjo-Iweala, n50 above, p3.

> development, market and economic conditions, the state of public finances and the institutional framework.[75]

In the case of Nigeria's oil subsidy removal policy, there are serious institutional and infrastructural issues which are not addressed by the SURE-P programme and which greatly impact on the sustainability of an economy that relies so heavily on its profits from oil. These issues include: the absence of a well regulated downstream oil sector; inefficient power generation and its adverse impact on entrepreneurship and investment; disregard for global concerns with renewable energy and climate change; and the pervasive corruption and absence of accountability in managing oil funds on the part of government and its agencies.

5.1 Absence of a well regulated downstream oil sector:

Removing oil subsidies without ensuring efficient refinery activity and a properly regulated marketing and distribution network of fuel to citizens at reasonable rates is false economy. The government may save misspending trillions on subsidies but if it does not address the regulatory and management deficits in its downstream sector operations, it loses even more than it gains. Without addressing the endemic problems with the subsidy regime referred earlier under the subsidy reinvestment programme, promises of infrastructural development do not satisfy the contention that an efficient regulatory framework for a commodity produced within the country can be efficiently subsidised for the benefit of all its citizens if managed properly.

5.2 Inefficient power generation and its adverse impact on entrepreneurship and investment:

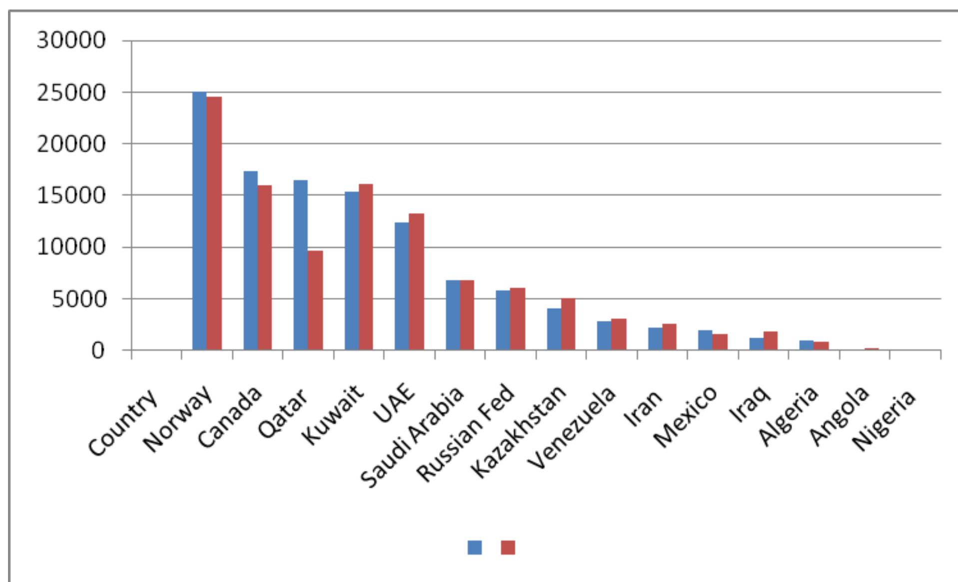
Entrepreneurship and investment activity, imperatives for a developing country's growth, are hugely dependent on efficient and regular power supply. Both the rich and poor require this basic access to electricity, if they are to engage in profitable business ventures for the benefit of the domestic economy. A much needed investment into the power sector in Nigeria may in our view, have proved to be a more efficient and visible objective of the oil subsidy removal policy. If we recall our pyramid showing the business strata in Nigeria in Figure 2, without

[75] Moltke et al, n30 above, 147.

dependable and reliable electricity generation, it is easy to see how the poor will continue to be worse off than the rich when the prices for the alternative source of power generation – petrol in generators, increases as a result of the subsidy removal.

The figure below comparing electricity consumption per capita in top oil producing countries, places Nigeria at the bottom of the table; a fact that ought to have been considered in determining how to redirect the funds recovered under the oil subsidy programme.

Figure 5: Progressive Electricity Consumption per capita (KWh) of top oil producing countries: Column 1(2005); Column 2(2012) (For table of data, see Appendix B)



Source: Compiled from various sources (Ezeani 2013) [76]

When one considers Nigeria's position as a top fuel producing and exporting country, the sustained poor refining capacity for crude, the wastage and environmental damage caused by gas flaring and by implication, the need for efficient gas utilisation projects;[77] and the poor

[76] The first column represents the top 15 producing countries in descending order of electricity consumption (regardless of mechanism for power generation). The data here is pulled from 2 distinct sources: the second column for the year 2005 is obtained from *ChartBin energy industry data* available at: http://chartsbin.com/view/2625, visited 12 March 2013, and the third for 2012 sourced from the CIA World Fact Book is available at: http://www.indexmundi.com/map/?v=81000 visited 12 March 2013.

[77] According to the World Bank for the period 2007-2011, Nigeria was the second worst offender after Russia, in recorded estimates from satellite data. Available at: http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTOGMC/EXTGGFR/0,,contentMDK:22137498~pagePK:64168445~piPK:64168309~theSitePK:578069,00.html visited 14 March 2013.

capacity of her hydro-electric power caused by poor maintenance of the Kainji dam facility, it is fair to challenge the absence of efficient power generation as a foremost objective in reinvesting funds from the subsidy programme. Infrastructural projects including hospitals and skills centres cannot operate without electricity and a country's capacity to produce and trade in competitive goods and in services, rest significantly on her power generation. Needless to say, Nigeria's position on this table relative to other oil producing countries in terms of electricity consumption for its citizens is unimpressive.

Efficiency in electricity provision could be achieved with better management of the Kainji Dam hydro-electric power project established in 1968.[78] The hydro-electric and renewable power generation project supplies Nigeria's major cities and Niger with electricity but maintenance has been neglected by successive governments and currently operates below capacity, resulting in the constant power outages the country is well known for. With the promise of even higher electricity prices for Nigerians in the future,[79] the broader question of efficient regulation of the power generation sector in Nigeria should also be a paramount consideration for the government in any reforms to the oil sector, including in considerations of projects that will be served by an oil subsidy re-investment programme.[80]

5.3 Disregard for global concerns with renewable energy and climate change:

The oil subsidy removal policy could also have factored in the global move towards alternative renewable energy sources. Two major markets for Nigeria's fuels, the US and the EU are pursuing these strategies. In the US for example, three legal instruments are relevant: the *US Energy Policy Act* 2005, the US *Energy Independence and Security Act* 2007 and Title IV (Energy and Water Development) under the *American Recovery and Reinvestment Act*

[78] See Ayegba Israel Ebije, 'An Inside Look at Kainji Dam' Daily Trust Newspaper 16 March 2011; online at: http://www.dailytrust.com.ng/index.php/feature/42904-an-inside-look-at-kainji-dam visited 4 March 2013. See also, Theophilus Abbah et al, 'Nigeria: Danger Looms at Kainji Dam' Daily Trust Newspapers 7 October 2012 online at: http://allafrica.com/stories/201210070325.html visited 4 March 2013.

[79] See Leon Usigbe and Gbola Subair, 'Prepare to pay more for electricity' Nigerian Tribune Newspapers 22 February 2013; online at http://tribune.com.ng/news2013/index.php/en/component/k2/item/5809-prepare-to-pay-more-for-electricity-fg-tells-nigerians-as-fg-phcn-successor-investors-sign-handover-agreements accessed 28 February 2013.

[80] The Nigerian Electricity Regulatory Commission (NERC) was established in 2005 under the *Electric Power Sector Reform Act (2005)* with the primary task of 'monitoring and regulating the electricity industry' – See NERC's web page at: http://www.nercng.org/index.php/about-us accessed 28 February 2013.

2009. The EU's *Energy Road map 2050*[81], projects an ambitious plan of decarbonisation, reduced dependence on fossil fuels by 2050, and energy efficiency. Under these strategies which are targeted towards reduced dependency on oil imports from countries including Nigeria, the implication for Nigeria who depends on oil exports for 90% of exports and 80% of her revenue[82] cannot be under estimated. Reforms in the oil sector including in oil subsidy removal programmes ought to factor in such considerations and make projections on how Nigeria's oil economy will not be adversely affected by a possible loss of businesses from its major importers. Government investment could also have been directed into research and development, to tackle the potential challenges that a reduction in oil exports may bring in the face of global moves towards decarbonisation.

5.4 Pervasive government corruption, the lack of managerial and administrative accountability, and disregard for the rule of law

A close read of the *Report of the Ad-Hoc Committee to Verify and Determine the Actual Subsidy Requirements and Monitor the Implementation of the Subsidy Regime in Nigeria*[83] produced and published by the Nigerian House of Assembly is profoundly shocking both for its indictment of government and for its revelations of the extent of mismanagement under the subsidy regime by all the parties involved. An overview of the findings in the Report is set out in the table below:

Figure 6: Mismanagement of the Oil Subsidy regime

BODY / AGENCY	NATURE OF DEFAULT UNDER OIL SUBSIDY REGIME
Nigerian Government	Corrupt approvals of invoices for payments; not empowering relevant agencies and parties (Nigerian Customs Service, Nigerian Ports Authority, Nigerian Navy, Nigerian registered vessels) the authority to act to prevent and counter smuggling.

[81] *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions Energy Roadmap 2050*, COM/2011/0855, 15 December 2011. Available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52011DC0885:EN:NOT visited 21February 2014.

[82] WTO: Trade Policy Review (Nigeria): Report by Secretariat *WT/TPR/S/247Rev.1*, 1 August 2011 at para 1, p1.

[83] n65 above. See in particular, Chapter 6, 72-184

Federal Ministry of Finance	Bad financial practices; outsourcing government work to unsupervised consultants who in turn acted negligently in their appraisal of quantities of oil imports.
Central Bank of Nigeria (CBN)	Poor FOREX policy which encouraged fraud by marketers.
Independent Inspectors of oil cargo	Negligence; collusion with marketers; no evidence of inspections.
Department of Petroleum Resources (DPR)	Lack of data; inefficiency; poor monitoring and poor supervision of licensees encouraging diversion and smuggling; no classification of products which meant consumers paid high prices even for inferior products supplied by marketers.
Petroleum Equalisation Fund Management Board (PEFMB)	Inefficiency; lack of real knowledge about the operations of the subsidy regime; no available data to show local product distribution.
Petroleum Product Pricing Regulatory Authority (PPPRA)	Self payment; arbitrary and illegal financial transactions.
Ministry of Petroleum Resources	Poor and negligent supervision of agencies in charge of the subsidy regime; conflict of interest in the role of Minister of Petroleum Resources who also acted as Chair of the Nigeria National Petroleum Corporation; abuse of powers of control over public funds contrary to SS 80; 162 of the Nigerian Constitution and the 2011 Appropriation Act.
Nigerian National Petroleum Corporation (NNPC)	Acting as importer, marketer, claimant, payer and payee in the subsidy transactions; non-accountability; lack of transparency in payment of subsidies contrary to Presidential directive; abuse of process; fraud (using depot owners with limited/no facilities for storage in order to create "artificial scarcity" in the country.
Independent Marketers	Exploitation of the lack of transparency and accountability in the subsidy regime.

Source: Interpretation of the findings in the 2012 Report of the National Assembly on the Subsidy Regime in Nigeria Report (Ezeani 2014).

By far the most alarming revelation for this research was the extent of collusion and outright corruption across the various government agencies which handled the subsidy payments. While the marketers were derided as corrupt, manipulative, greedy business men and women hence the 'rich' who were benefitting at the expense of the poor, the real culprits appear to

have been the government ministries, agencies, parastatals, auditors, security operatives, and to an extent the Central Bank, who were involved directly or indirectly in overseeing and managing the oil subsidy scheme. From the table above, the only body which was relatively devoid of malpractice although its competency in fiscal policy making with regard to FOREX transactions by the independent oil marketers was questioned, was the Central Bank of Nigeria.

6. Conclusion

The foregoing review of the necessity or false economy of removing oil subsidies proves the theory against retention of oil subsidies is right to an extent. In Nigeria, oil subsidies may have helped the marketing and distribution of oil products. The subsidy regime however did not guarantee against adulterated products entering the market, the absence of scarcity of oil products, and fostered fraudulent market activity. Nevertheless, we have shown that the *removal of oil subsidies* requires more than simple government fiat and a grand policy of reforming institutional and infrastructural deficiencies, the latter of which ought to be a paramount concern for any government in any event. In our view, oil subsidy removal policies adopted without a thorough consideration of the domestic market and its needs amounts to false economy. Removing oil subsidies may mean savings but it will not remove the prevailing problems of maladministration in the oil sector of a domestic economy, of its own accord.

Oil subsides may 'distort the market' but they are only able to do so because they are protracted, poorly regulated, and administered inefficiently. It is this inefficiency that informs the corruption and the distortion which ultimately leave the poor worse off, with both the wealth and the oil in the hands of those few who can operate the licences for marketing and distribution of oil products. The gross mismanagement and poor regulation of the Nigerian oil subsidy scheme left it open to mismanagement, illegalities, and outright fraud. The fact that the subsidies were in the form of direct monetary payments to those engaged in the business of marketing and distribution made it even easier for government agencies to make illegal and arbitrary payments to themselves, and for private persons to profit from the loopholes in the scheme. Although this is no guarantee against mismanagement, a more sophisticated indirect subsidy payment in the form of properly regulated tax exemptions, or other non-

monetary incentives including assistance with building storage facilities, reduced charter rates for the use of Nigerian vessels, reduced import duties and port charges, may have been more appropriate to check the ease of illegal financial transactions and improve accountability. A clear time line for the grant of subsides in the oil sector and a strategy for when the subsidies are to be reviewed or ended would also have been of benefit; without any duration for the scheme, it also meant that those who profited from its mismanagement would be only interested in perpetuating its exploitation.

Hence a policy to remove oil subsidies may be a necessity satisfied by observations in theory but it will only avoid being false economy if it is implemented appropriately and sustainably. Such a policy must be well planned and well executed, with an accurate identification of those broader contextual issues that led to, and amplified the negative consequences of a badly administered, indefinite, and poorly regulated oil subsidy scheme. To do otherwise would be a double loss to the economy: inefficient oil subsidy payments with no lasting legacies for the benefit of the country compounded further by inefficient subsidy reinvestment plans which do not address necessary and broader areas of reform or suggest a strategy to stimulate growth or development in the oil sector and in the wider economy of a developing country.

Appendix A: [See Figure 1; n47]

Table 1: Comparison Tables – Top Oil Exporting countries and Consumer Prices for most widely sold gasoline products 2008-2012

Country	Pump Price (per litre) USD	Rate in ₦ (155 per USD)
Norway	2.12	328
Canada	1.21	187
Russian Fed	0.84	130
Mexico	0.81	125
Iraq	0.78	120
Kazakhstan	0.71	110
Angola	0.65	100
UAE	0.47	72
Nigeria	0.44	68
Algeria	0.32	49
Kuwait	0.23	35
Qatar	0.19	29
Saudi Arabia	0.16	24
Iran	0.10	15
Venezuela	0.02	3

Appendix B: [See Figure 5; n82]

Table 5: Progressive Electricity Consumption per capita (KWh) of top oil-producing countries: Column 1(2005); Column 2(2012)

Country	Electricity consumption per capita (KWh) **2005**	Electricity consumption per capita (KWh)) **2012**
Norway	25090.2	24557.7
Canada	17321	16020.3
Qatar	16453.9	9628
Kuwait	15347.9	16090.3
UAE	12411.6	13281
Saudi Arabia	6813.3	6813.3
Russian Fed	5786.4	6017.4
Kazakhstan	4071.7	5029.5
Venezuela	2848.4	3060.8
Iran	2142.5	2620.8
Mexico	1953.5	1578.5
Iraq	1153.6	1788
Algeria	898.6	816
Angola	142.3	186.3
Nigeria	136.1	106.6