

NOC Reform in Iraq

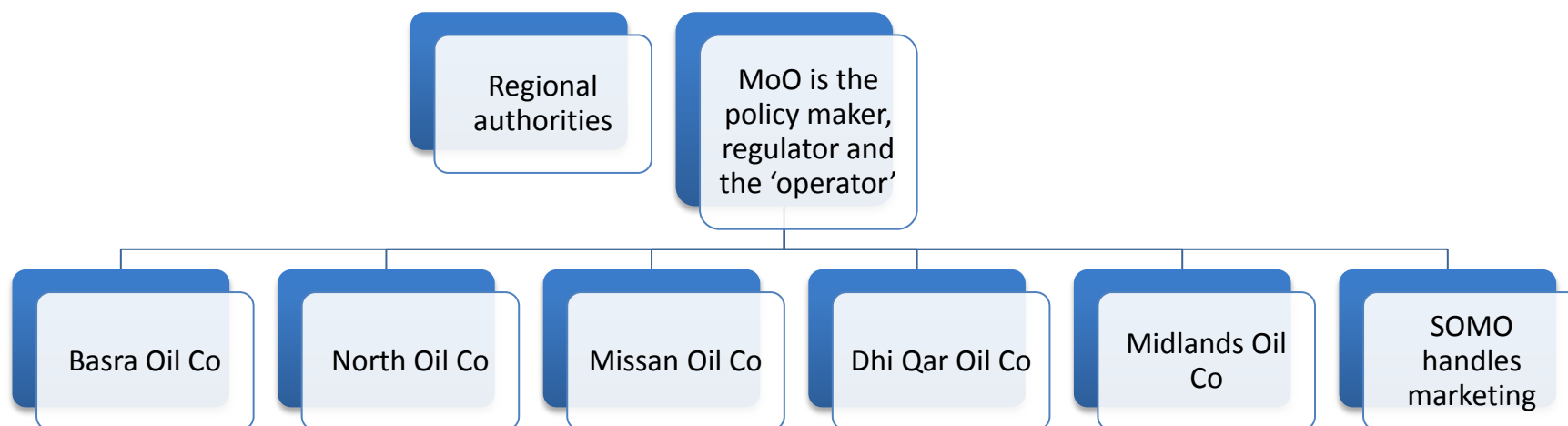
Dr Valérie Marcel, Associate Fellow, Chatham House

Iraq Energy Forum, Baghdad, 2 April 2017

Current policy question

- Ministry of Oil drive to reorganise and restructure its operations
- Iraq is working to re-establish the Iraq National Oil Company (INOC) (as well as a national gas company and a national refining company)
- What are the options?
- Which make the most sense in Iraq?

State of affairs



Some of these companies are well established and used to their autonomy.
Regional oil companies sell directly to SOMO (profit centres)

Parent company vs. Loose regional NOC system

Benefits of central coordination

Uniform standards for accounting, audit, disclosure
=> Reduces corruption

Standard decision-making processes => Reduces risk

Centralize core functions =>
Reduce duplication & waste,
Increase coordination

Benefits of regional/operational level autonomy

Giving regions more control over project decision making
=> Regional buy in

More input from operations in planning

Reduces burden on MoO

Centralized and coordinated looks like a winner

But there are dangers too

- Not well implemented
 - Some companies continue to operate under business as usual model
 - Some regional authorities fight the loss of responsibilities over strategy making and planning
- ➔ Confusion, affecting operations and increasing corruption risk

Keys to successful reform

- Representative/inclusive leadership at MoO and INOC
- High standards of governance to increase trust in centralised structure

Core governance principles: The Chatham House Document

	Chatham House Governance Principle	Key NOC Questions
1	Clarity of goals, roles and responsibilities	What is the NOC's role? Is it clearly delineated vis-à-vis other organisations?
2	Enablement to carry out the role assigned	What is the NOC's financing model and how much autonomy will it have?
3	Transparency and accuracy of information	What information will the NOC be required to report and how will it be verified?
4	Accountability of decision-making and performance	How will performance be assessed? Who has authority over NOC?
5	Sustainable development for the benefit of future generations	How will the NOC contribute to sustainable development from an exhaustible resource?

Clear roles, goals and responsibilities

- Who does what?
 - Regulations ✓
 - Policy
 - Strategy
 - Planning

Most common confusion: policy and strategy

Clarify limits of responsibility of the Ministry of Oil and the Regional Authorities, INOC and regional companies in making policy, strategy and operational plans. Otherwise competing centres of powers will lead to confusion in decision-making.

Governance system impacts NOC performance

Fragmented authority

KPC, NIOC, NNPC, PEMEX

Actors wrestle with each other for authority. Roles are not clear.

=) Negatively affects NOC performance.

Centralized authority

ADNOC, GAZPROM, PDVSA, PETRONAS, ARAMCO, SONANGOL, STATOIL, PETROBRAS

=) Leads to better performing NOC – except PDVSA + Gazprom because of lack of clarity of roles there.

Source: Victor, Hults, Thurber (2012), Oil and Governance

Enablement of INOC and regional companies

- Clear mandate and oversight
- Managerial autonomy
- Capacity-building
- Clear financial model that provides NOC with funds to deliver strategy



NOCs need incentives for cost control

If INOC sells crude to the Oil Marketing Company based on “delivery price” and a “reasonable profit” = cost plus system.

Risks:

- 1) With “delivery price” no incentive to keep costs low
- 1) Who determines what’s “reasonable”? And how?

(This problem is the same if the regional oil companies sell on a cost plus system)

Cost auditing = another important driver for NOC cost control

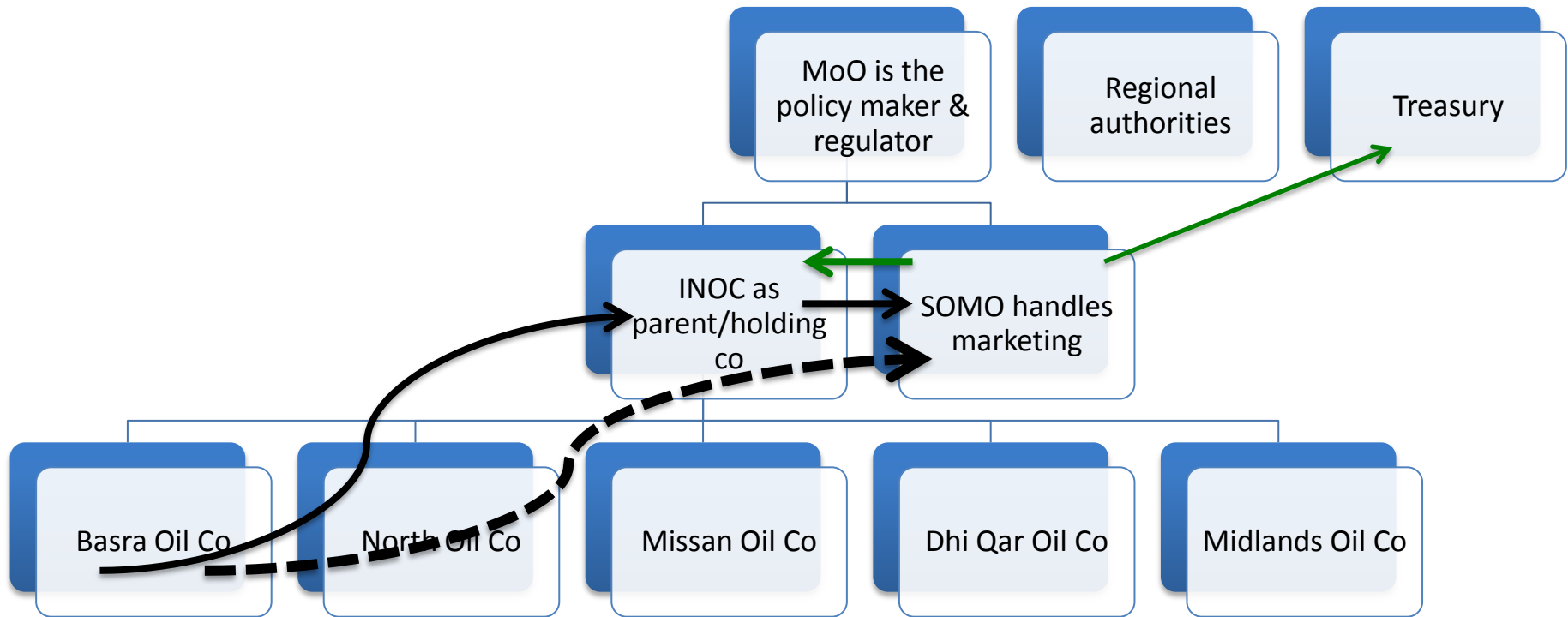
Some key questions to consider in NOC restructuring

How are financial and feedstock transfers between companies accounted for?

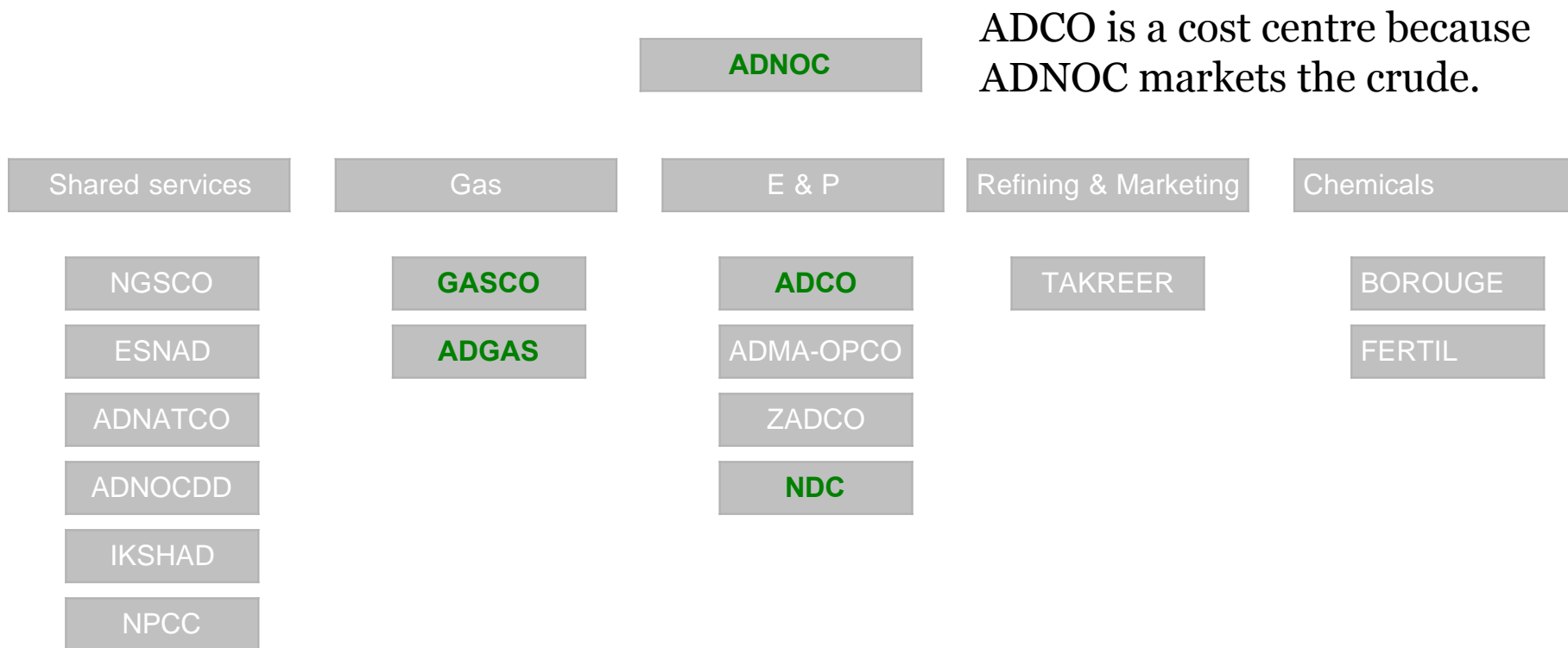
What subsidiaries will function as cost and profit centers?

Functional or regional subsidiaries? Or both?

Introducing INOC into the system



Centralised budgeting overcomes cost/profit centre problem



But transfer pricing is where it can get murky. Need clear view of how well each subsidiary/company is doing.

In the case of GASCO pays an 'internal price' for gas that is accounted for in its annual report (not for public view)

Partial listing on public stockmarkets

- Benefits (e.g., KSA objectives)
 - Raise finance
 - Focus on profits (cut costs)
 - Wider public ownership (if local capital available)
 - More transparency
 - More autonomy from political interference
- Difficulties
 - Ringfencing the unprofitable part of the business (subsidies, transfer pricing, bloated workforce)
 - Saudi Aramco (and Pemex)

Conclusion

- Restructuring NOCs = opportunity to improve corporate processes
- Needs clarity
- Simple systems make it easier to hold organisations to account

Thank you

For further information, please contact Dr Valerie Marcel,
vmarcel@chathamhouse.org