# Royalty Interest Management Strategy, Cost Implications and Financial Performance of Oil and Gas Companies in Niger Delta

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**ABSTRACT**
The study examines royalty interest management strategy, cost implications and financial performance of oil and gas companies in Niger Delta with the purpose of finding out if denial, payment to selected community leaders and divide and rule relate to profitability. In carrying out the study, data was collected from 38 respondents through the issue of structured questionnaire and the data collected was analyzed adopting pearson correlation and regression analysis methods. From the analysis, we found that denial and divide and rule are not statistically significant in explaining the profitability of oil and gas companies and in the other hand, payment to the selected community leaders was statistically significant in explaining profitability. Based on the findings, we recommend among others that government should restore confidence to the peoples of the Niger Delta that they can be partners in progress.
***Keywords:*** *Royalty interest; Cost Implications, Denial, divide and rule*

## INTRODUCTION

Royalty is the remuneration payable to a person in respect of the use of an asset calculated by reference to and varying with quantities produced or sold as a result of the use of the asset. The owner of the asset is generally referred to as landlord while the user is referred to as the Tenant. Royalty comes in different forms which are; Mining royalty which is based on ore raised, patent royalty which is based on product sold and copy right royalty which is based upon books sold. In handling issues concerning royalty, certain terms are applied which include; royalty payable which has to deal with amount calculated based on the quantities produced and sold. The higher the quantity sold or produced, the higher the royalties payable. Minimum rent which is the guaranty (lowest) sum payable to the landlord. Royalty paid which is the amount actually paid to the landlord in any month, which is the higher of the royalty payable and minimum rent (Aborode, 2006). For the purpose of this paper, we shall be limited to mining royalty.

The issue of how to improve organizational performance has been a major area of active research in recent times. Most organizations have adopted different strategies aimed at improving organizational performance. However, inspite of the efforts made by organizations to improve their efforts have remained futile. The reason behind this is not far fetch as most organizations which in the context of this study are oil companies, communities in Niger Delta and government of Federal Republic of Nigeria have failed to recognize and attach much importance to management development, because they have failed to recognize and attach much importance to management practices for better performance (Ibrahim, 2010).

There are three major groups that have interest in the royalties which are involved in the crises in the Niger Delta, they are Nigerian state, the oil companies and the communities in the Niger Delta. The Nigerian state has maintained over the years that the crisis in the Niger Delta has been issue of security. The government feel that the essence of the crisis has to be in line with the breakdown of law and order in the Niger Delta because of oil extraction activities. The Nigerian state support that the crisis in Niger Delta is as a security, it has drawn attention to communal activities against oil companies, activities of militants, murder of state security personnel and murder of oil workers. To back the allegations up, the UNDP in 2006 Report of the Niger Delta adopted the government position and suggested that the people in the Niger Delta are known for war and conflict, and for that, security problem has always existed in the Niger Delta. Hence, for the Nigerian State, the truth concerning the crisis in the Niger Delta is refusal of individuals, groups and communities in the Niger Delta to accept its definition of the situation and engage in acts of resistance (Iyayi, 2008).

In the Niger Delta, there are six major oil companies of which Shell enjoys the highest position in terms of activities arising from oil drilling. All these oil companies are of the view that the crisis in the Niger Delta is evidenced from the opposition the oil companies are getting as they carry on their legitimate activities, because the oil companies think along side the Nigerian state in their drawing attention to communal activities against them, the activities of the militants, attacks on and destruction of oil facilities and vandalisation of pipelines by armed gangs, hostage taking and murder of oil workers etc.

The position of the Niger Delta communities in relation to the crisis has to do with the injustice in connection with issues surrounding oil extraction activities and appropriation of the huge oil revenues that lies at the heart of Niger Delta crisis. The communities point to the weak regime of rules and regulations that govern oil extraction, the environmental tragedies in the Niger Delta, the murder of the rights and nationality leaders and the massive poverty in the Niger Delta, all these are backed up with the World Bank Reports by Singh, Moffat and Linden (1995), that despite Niger Delta vast oil resources, the region remains poor.

Several studies have been conducted on issues concerning oil and gas and related crisis in Niger Delta (e.g. Davies S.D. et al 2014, Harvest Major and Jonathan Adejoke 2013). However, most of the studies conducted focused on Niger Delta crisis arising from oil and extraction in Niger Delta, and non on Royalty interest management strategy, cost implications and profit of oil and gas company in the Niger Delta. It is in view to fill this gap in literature that prompted this study. In the context of this study royalty interest management strategy shall be measured by denial, payment of money to selected leaders, Divide and rule, marginalization and violence while financial performance shall be measured by profitability.

**RESEARCH PROBLEMS**

In this paper, it is necessary to note that a lot of factors account for the problems in the Niger Delta. These include environmental degradation, poverty and lopsided government legislation as they affect oil companies. The people of the region have suffered major neglect over the years despite the fact that this region has contributed to the economic growth of Nigeria.

Noticing all these problems the federal government of Nigeria have resorted to intimidation, harassment in responding to crisis in Niger Delta because in most cases, the government reacted to crisis through the use of instruments of state violence to harass agitations and environmentalists in the region. In 1992 October, Umuechem people in Rivers state protested against Shell Petroleum Development Company because of discrimination in the hiring of unskilled workers as well as absence of basic amenities in their community in a peaceful manner, but it became violent when the Shell Petroleum Development Company (SPDC) brought in the mobile police squad. The whole thing ended tragically for the people of Umuechem because on November 1, 1992, the whole community was leveled to the ground causing the live of the traditional ruler and hundred of others were either maimed, assaulted and raped (Aghalino, 2004).

While it is arguable that the federal government has demonstrated a clear attempt to positively attend to the problems emanating from oil exploration and production, it has in most cases, responded to the crisis through the use of instruments of state violence to harass agitators and environmental whistle blowers in the region.

Example of this pattern of response was replicated for the Ilaje people on May 25 1998, a number of Ilaje people in Ondo state started a peaceful demonstration when all efforts to have a meaningful dialogue with Chevron and Government failed. On 28th of May, three helicopters loaded with soldiers came to the barge where Ilaje representatives were waiting for Chevron teams. The solders started shooting before the helicopters even landed to disperse the people. A number of casualties were recorded (Naanen, 1995). It is in view to address this problem that prompted this study.

**THEORETICAL FRAMEWORK**

This study was based on the following theories: Hubbert Peak, Social contract, quality of life and positive accountancy.

**Hubbert Peak Theory**

Hubbert Peak theory on royalty interest of the view that maximum production from an oil reserve will occur towards the middle of the reserve life cycle. The theory further suggests that the production rate from a region follows a bell shape pattern and that the region could be a country or a noticed oil field (www.investopedice.com/terms/h/hurbbert-peak-theory.asp).

**Social Contract Theory**

According to Ketznelson (2008) social contract theory and quality of life theory hold the notions that sovereignty resided in the people for whom governments were trustees and that such government could be legitimately over thrown if they failed to discharge their functions to the people. Ramanathen (1976) said that the relationships of social contract theories is seeing a company as an integral part of the society, support and follow the law of that society. It is needed that they contribute to the society proportionately enough to what the society has given them.

**Quality of Life Theory**

In the same vein, quality of life theory is almost the same expectation unrestrained economic development noticed form environmental pollution and social ills gingered society's negative attitude towards industrialization which is connected to environmental pollution and social ills and therefore seen to reduce quality of life and increase social costs. The extent to which an organization balances back the quality of life of people in the environment where it operates is a yard stick for proper measurement.

**Positive Accounting Theory**

The Positive Accounting Theory (PAT) from Walts and Zimmerman (1986) see (organization and company) as a means of codifying contracts which are necessary in order to get self-seeking individuals to agree to corporate. The contracts are necessary to get individual parties to act to maximize the wealth of the owners (shareholders) nevertheless, there will be contracting cost associated with contracts. Example, cost of negotiating, maintaining and monitoring the performance of the parties involved. Positive accounting theory maintaining that firms will seek to minimize the contracting costs and this will affect the policies adopted as well as the accounting policies (Graffikin, 2007) Watts and Zimmerman 1986) hold the view that the objective of positive accounting theory is to describe, explain and predict accounting practice of managers, so that it will be clear which firm publishes certain information like corporate disclosure but positive accounting approach says nothing about which method of reporting should be used as a positive theory is based on empirical information and is not normative.

## MANAGEMENT STRATEGIES

In order to support the view that the crisis in the Niger Delta is the result of opposition to their legitimate activities, the oil companies like the Nigerian state drew attention to: communal activities against them, activities or militants, attack on and destruction of oil facilities and vandalization of pipeline by armed gangs, hostage taking and murder of oil workers. To deal with this opposition and end the crisis, the oil companies have adopted a variety of strategies including:

Deployment of massive propaganda, payment of little or no compensation, massive bribery of officials of the Nigerian state, relocating their corporate headquarters to places far away from the crisis, temporarily shutting up operations, adoption and deployment of various community relations strategies that involves denial, silence, blaming the victim, defiance and a “wallpaper factory mentality” (Iyayi, 2000).

In the issue concerning divide and rule method the oil companies adopted, Ashton-Jones (1998) pointed out that the activities of global oil companies are framed within an entrenched oil industry culture that is founded on some assumptions:

That profit maximization is the only basis upon which a company can run, so that any expenditure beyond what is required to get out the oil is resisted. That a deal can be made with governments only, regardless of the governments legality or morality. That once an arrangement has been made with a government, a mining company can do what it likes, in fact, to act as it is a government agency. That the “Market” has a right to have the resources it wants, at the lowest price, and regardless of the cost to local people who obliged to play host to mining companies and that “we” the mining companies, know best and are acting responsibly.

## RESEARCH PURPOSE

The purpose of the study is to examine royalty interest management strategy, cost implications and financial performance of oil and gas companies in Niger Delta. The specific objectives of the study are as follows:

(1) To determine the extent denial as a royalty interest management strategy relates with profits of oil and gas companies in Niger Delta.

(2) To determine the extent payment to selected community leaders as a royalty interest management strategy relates with profit of oil and gas companies in Niger Delta.

(3) To determine the extent divide and rule as a royalty interest management strategy relates with profits of oil and gas companies in Niger Delta.

## HYPOTHESES

$Ho_1$: There is no significant relationship between denial as a royalty interest management strategy and profitability of oil and gas companies in Niger Delta.

$Ho_2$: There is no significant relationship between payment to selected community leaders as a royalty interest management strategy and profitability of oil and gas companies in Niger Delta.

$Ho_3$: There is no significant relationship between divide and rule as a royalty interest management strategy and profitability of oil and gas companies in Niger Delta.

## METHODOLOGY

This study adopted the quasi experimental survey design since the variables of the study are not under total control of the researchers. The target population for this study comprised all oil and gas companies workers in oil and gas companies in Niger Delta, government agents and members of the host communities. However, due to the difficulty of conducting a successful study on the entire population, consequently, the accessible population made up of workers of oil and gas companies, government agents and the host communities in Rivers State. Adopting purposive sampling procedure method. 40 persons were chosen for the study. The instrument used to gather data was royalty interest management strategy, cost implications and Financial Performance Questionnaire (RIMSCIAFPQ) constructed by the researchers. It was divided into sections A which took care of personal data, section B took care of the variables of the study arrange in likert format of strongly Agree (4), Agree (3), Disagree (2) and strongly disagree (1). The main variables of the study are: The independent variable which is royalty interest management strategy was represented by denial, payment of money to selected leaders and divide and rule method while the dependent variable which is financial performance was represented by profitability and simple regression and correlation analysis were used for the study.

The face and content validities were ascertained by scrutiny from experts in accounting. Their suggestion were incorporated to improve the quality of the instrument. The instrument was pilot tested by 10 accountants that were not part of the study. To establish the reliability of the instrument for this study, the researcher employed Kuder Richardsons formula 21 (k-R 21) to compute the coefficient of the reliability, the reliability gave a result of 0.87 that made the instrument reliable for usage in this study.

## DATA ANALYSIS PROCEDURES

In this study, the data collected was analysed using Pearson Correlation and Multiple Regression Analysis.

The correlation analysis was used to investigate the individual relationships of the independent variables to the profitability of oil and gas companies in the Niger Delta. From our results, it is evident that of the three independent variables, only Denial as a Royalty Interest Management Strategy was positively correlated with financial performance of the oil and gas firms sampled. This implies that the adoption of Denial is expected to lead to increased profitability of the firms.

However, making Payments to Selected Community Leaders (PSCL) is indicated to likely lead to decreased profitability. The same thing also applies to trying to using Divide and Rule (DR) as a Royalty Interest Mgt Strategy.

### Hypothesis 1:

There is no significant relationship between using Denial as a Royalty Interest Mgt Strategy and profitability of oil and gas companies in the Niger Delta.

From our regression results in table 1 above, the computed t-statistic for the coefficient of Denial as a Royalty Interest Mgt Strategy is 1.638 which is lower than the critical t-statistic of 1.68 at 0.05 level of significance. This means that the null hypothesis is accepted. Thus, we accept that there is no significant relationship between using Denial as a Royalty Interest Management Strategy and the Profitability of Oil and Gas Companies in the Niger Delta.

### Hypothesis 2:

There is no Significant Relationship between Payment to Selected Community Leaders as a Royalty Interest Management Strategy and the Profitability of Oil and Gas Companies in the Niger Delta.

From our regression results in table 2 above, the computed t-statistic for the coefficient of Payment to Selected Community Leaders as a Royalty Interest Management Strategy is 3.541 which is higher than the critical t-statistic of 1.68 at 0.05 level of significance. This means that we reject null hypothesis and accept that there is a Significant Relationship between Payment to Selected Community Leaders and the Profitability of Oil and Gas Companies in the Niger Delta.

### Hypothesis 3:

There is no significant relationship between Divide and Rule as a Royalty Interest Management Strategy and the Profitability of Oil and Gas Companies in the Niger Delta.

From our regression results in table 2 above, the computed t-statistic for the coefficient of Divide and Rule as a Royalty Interest Mgt Strategy is 0.970 which is lower than the critical t-statistic of 1.68 at 0.05 level of significance. This means that the null hypothesis is accepted. Thus, we accept that there is no significant relationship between Divide and Rule as a Royalty Interest Mgt Strategy and the Profitability of Oil and Gas Companies in the Niger Delta.

 

**Data Analysis and Interpretation**
**Table 1**

**Correlations**

| | | PRF | DENIAL | PSCL | DR |
|---|---|---|---|---|---|
| Pearson Correlation | PRF | 1.000 | .354 | -.534 | -.237 |
| | DENIAL | .354 | 1.000 | -.150 | -.302 |
| | PSCL | -.534 | -.150 | 1.000 | .053 |
| | DR | -.237 | -.302 | .053 | 1.000 |
| Sig. (1-tailed) | PRF | . | .016 | .000 | .079 |
| | DENIAL | .016 | . | .187 | .035 |
| | PSCL | .000 | .187 | . | .378 |
| | DR | .079 | .035 | .378 | . |
| N | PRF | 37 | 37 | 37 | 37 |
| | DENIAL | 37 | 37 | 37 | 37 |
| | PSCL | 37 | 37 | 37 | 37 |
| | DR | 37 | 37 | 37 | 37 |

**Table 2:**

**Coefficients[a]**

| Unstandardized Coefficients | | Standardized Coefficients |
|---|---|---|
| B | Std. Error | Beta |
| 29.380 | 5.560 | |
| .222 | .136 | .238 |
| -.208 | .059 | -.491 |
| -.102 | .105 | -.139 |

a. Dependent Variable: PRF

**DISCUSSION OF FINDINGS**

From our findings, denial as a royalty interest strategy was positively correlated with profitability, this implies that the adoption of denial is on the short run expected to lead to profitability. That supports (Iyayi, 2000) that oil companies adopt this method to enhance their profit. But, the regression result shows that denial is not statistically significant in explaining the profitability of oil companies.

Our result shows that payment to selected community leaders is negatively correlated with the profitability of the oil companies, the implication of this, is that money paid to community leaders tend to negatively affect profitability, because this money paid to few community leaders may totally generate problems which may lead to long time fueled crisis and reduce the profit (Iyayi 2000).

The strategy of divide and rule shows a negative correlation with profitability, the implication of this findings is that as companies adopt divide and rule as a strategy, will tend to reduce their profitability, which supports Ashton-Jones (1998).

**CONCLUSION**

From the findings of the study, we conclude that denial does not significantly affect profitability of oil companies. Payment to selected community leaders significantly affect profitability negatively and finally divide and rule does significantly affect profitability.

**RECOMMENDATIONS**

Considering the need for the Nigerian state, oil companies and the communities to make positive progress in the Niger Delta, the researchers recommend as follows:

- There is need to restore the confidence of the peoples of the Niger Delta by showing that Nigeria state and oil companies can be partners and not enemies in the development of the Niger Delta.
- Conducting credible elections that will usher in good governance at all levels, local government, state and federal level.

- There is need for the government to discourage the oil companies to use denial, divide and rule strategies as operational strategies.

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