A Legacy of Liability

Shell and the Niger Delta

Introduction

The UN Environment Programme (UNEP) published a report on 4 August 2011 outlining the findings of an independent and comprehensive study of oil pollution in Ogoniland in Nigeria. The report exposes an unacceptable legacy of pollution exposing local communities to contaminated groundwater and soil. It also exposes a consistent failure on the part of Royal Dutch Shell’s Nigerian subsidiary, Shell Petroleum Development Company (SPDC), to meet its legal obligations to clean up oil spills promptly and properly.

The report’s findings support the view that SPDC has created a legacy of undisclosed liability for the company through its failure to comply with its legal obligations to clean up oil spills. This failure has exacerbated clean up costs which remain the legal responsibility of the relevant operator (SPDC in many instances). The report also questions the adequacy of Shell’s remediation process (RENA) calling for a full review and ‘overhaul’ of the company’s oil spill and remediation procedures.

Although the UNEP report deals only with Ogoniland, its findings of systemic failings and its recommendations are relevant to SPDC’s other operations across the Niger Delta. If similar problems do exist across the Delta potential financial liabilities for clean up and, in cases of operational spills, compensation could be significant.

To date, neither SPDC nor Shell has disclosed the cost of actual or anticipated clean up in the Niger Delta. This creates an information vacuum for investors. The significance of these potential financial liabilities can be gauged from the UNEP recommendation that $1bn is set aside for the first 5 years of a 30 year clean -up project in Ogoniland alone.

This investor briefing provides a summary of the UNEP report’s findings and recommendations as they relate to SPDC and SPDC’s response. It examines the risks facing the Shell group and shareholders as a result of these findings. Finally we propose suggestions for investor engagement with Royal Dutch Shell on the UNEP report.

Oil Spill Comparisons

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<tr>
<td>Gulf of Mexico</td>
<td>4.9 million barrels</td>
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<tr>
<td>SPDC Niger Delta spills (1998-2010 only)</td>
<td>519,207 barrels</td>
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<td>Exxon Valdez</td>
<td>257,000 barrels</td>
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Royal Dutch Shell: Key Data

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<tr>
<td>Global Production</td>
<td>3.3 million</td>
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<td>(Barrels of oil</td>
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<td>equivalent / day)</td>
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<tr>
<td>Nigeria Oil Production</td>
<td>302,000</td>
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<tr>
<td>SPDC Nigeria oil</td>
<td>519,207</td>
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<tr>
<td>spill volume 1998-</td>
<td>barrels</td>
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<td>2010</td>
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The UNEP Report

• Published on 4th August 2011.
• An unprecedented assessment over a 14-month period.
• Examined more than 200 locations, surveyed 122 kilometres of pipeline rights of way, reviewed more than 5,000 medical records and engaged over 23,000 people at local community meetings.

Key Findings of the UNEP Report

1. Systemic and serious failures in SPDC’s clean up of oil spills

The report provides evidence that SPDC’s remediation processes are inadequate, unsuited to Ogoniland and in need of review and overhaul. This may have implications for the company’s wider Nigerian operations. The report also provides evidence that SPDC is inaccurately recording spill sites as having completed remediation. This failure to clean up means that such costs are yet to be incurred by the company and indeed such costs will likely be increased by the delay. Specific findings include:

• Ten out of the fifteen sites investigated by UNEP which SPDC records show as having completed remediation, “still have pollution exceeding the SPDC (and government) remediation closure values.” Contamination at 8 of those sites has spread to groundwater.

• Remediation by enhanced natural attenuation (RENA) has not proven to be effective. UNEP find that the RENA process is “failing to achieve either environmental clean-up or legislative compliance.” It goes on to say that “it is also failing to achieve compliance with SPDC’s own procedures.” A new remediation management system introduced by all Shell companies in Nigeria in January 2010 was found to be an improvement but still does “not meet the local regulatory requirements or international best practice”.

2. Inadequate control, maintenance and decommissioning of oilfield infrastructure

The report finds that neither industry best practice nor SPDC’s own procedures have been applied, creating public safety issues.

UNEP Recommendations for SPDC

1. To fully review and overhaul procedures for oil spill clean-up and remediation as well as improve on contracting and supervision.
2. To conduct a comprehensive review of SPDC assets in Ogoniland and develop a decommissioning programme and Integrity Management Plan for the assets.
3. To work with Nigerian regulators to clarify the legislation governing intervention and target values.

UNEP also made a recommendation for the establishment of an environmental remediation fund with an initial amount of $1bn to be paid by industry operators and the Nigerian federal government. Royal Dutch Shell states in its 2011 Annual Report that “SPDC immediately accepted the full recommendations of the UNEP report.”

However, a review of the SPDC response raises questions about this statement.

SPDC’s initial response to the UNEP report is available at:
http://www.shell.com.ng/home/content/nga/environment_society/our_response/
SPDC responds to each of the three UNEP recommendations set out above.
Risks for Investors

Financial Impact on SPDC

Clean up costs

Too often discussions on the cost of oil spill clean up become diverted by an argument over the cause of spills. In terms of financial impact the cause of a spill is relevant only to the extent that compensation is payable by SPDC for operational spills only. However, SPDC is liable for the financial cost of clean up of oil spills regardless of the cause of such spills.\textsuperscript{13}

Although Shell discloses oil spill volume in Nigeria, it has not, to date, made any disclosures regarding incurred or potential clean up costs.

The UNEP report suggests that clean up has been inadequate and the passage of time has exacerbated clean-up costs through the further spread of contamination. Both the Nigerian and Dutch governments have made statements recently indicating that they expect greater action by the Shell group in cleaning up spills and improving asset integrity suggesting that SPDC will incur costs for clean up and improving and decommissioning infrastructure.\textsuperscript{14}

Questions for Shell

- Will the company disclose the costs of clean up and remediation of spills in addition to the volume of oil spills?
- What has been the cost of oil spill clean up and remediation in the Niger Delta to date?

SPDC has confirmed that it will “revisit the sites in Ogoniland investigated by UNEP to determine whether clean up and remediation have been adequate, and take action as required.”

The UNEP team has already independently determined that clean up and remediation has been inadequate at a number of sites. As delays have already exacerbated clean up costs which SPDC will incur, it would seem prudent for the company to determine what action should be taken at this point to clean up and remediate the sites rather than conduct another investigation into whether remediation has been adequate.

Questions for Shell

- What steps are the company taking to ensure prompt and proper clean up of the 10 sites identified by UNEP to international best practice/Nigerian regulatory standards, with independent verification of that clean up?
- What are the estimated costs of such clean up?

Costs of asset integrity management and decommissioning

SPDC has stated it is committed to “an asset integrity management plan for Ogoniland”. It emphasises the importance of community and government support and the “unique challenges regarding access to Ogoniland”. SPDC confirms that it has set up a team to review and develop a comprehensive decommissioning programme and asset integrity plans and “looks forward to discussing these plans with the relevant Ogoni communities.”
A lack of access is often cited by SPDC as a key factor in its failure to clean up spills and decommission facilities. It is important that we deal separately with situations where access has been available but company actions have been inadequate on the one hand and issues of a lack of access on the other. For example, the UNEP report refers to 15 sites which SPDC had access to and which the company claimed had completed remediation. This was found not to be the case in 10 of those sites. Failure to clean up and remediate those 10 sites therefore was not linked to a lack of access. The UNEP report also noted that “there was always a time-lag between the spillage being observed and dealt with…” and that the “time-lag between the spill event and the site being comprehensively cleaned up shows that issues of access are not the sole cause of delays.” Accordingly, it is clear that lack of access is not at the heart of many of the SPDC failures identified by UNEP.

This is not to suggest that access is never an issue. SPDC has a troubled history in Ogoniland linked to the death of Ken Saro Wiwa which eventually led to the company having to abandon production in the region. Shell’s social license to operate in the region has been irretrievably damaged owing to a lack of trust among local communities. It is therefore essential that Shell works together with other stakeholders to determine an appropriate way forward. Various options should be considered including a centralised clean up mechanism to which all industry operators contribute which may alleviate company specific access issues.

Questions for Shell

What is the timetable for reviewing and developing a decommissioning plan?

What are the anticipated costs in decommissioning facilities?

What steps is the company taking to ensure the support of the Ogoni communities? Will the timetable for a decommissioning plan and anticipated costs be publicly disclosed?

Reputational Impact on Royal Dutch Shell

Royal Dutch Shell has faced sustained criticism from NGOs and community groups for its Nigerian operations. Two formal complaints have been filed by Amnesty International and Friends of the Earth International under the OECD Guidelines for Multinational Enterprises. Amnesty International has issued a public memorandum criticising SPDC’s public response to the UNEP report and the continuing delay in undertaking clean up. NGOs have expressed frustration at Shell’s seeming reluctance to accept in full the findings of the UNEP report. Amnesty has described SPDC’s statement that “SPDC agrees with the UNEP finding that all sources of ongoing contamination, including activities such as crude theft and illegal refining, must be brought to an end before an effective widespread clean up can begin” as “both incorrect and indefensible.” This is because the UNEP report makes clear that in the case of land contamination (as opposed to water contamination) “The potential for future spillages, either from operational accidents or illegal activities, should not preclude the decision to initiate clean up action where the source and extent of contamination are known.”

A number of investors are facing calls to disinvest from Royal Dutch Shell on environmental and human rights grounds. This public action is likely to continue, making it imperative that Royal Dutch Shell addresses the issues identified by the UNEP report and implement appropriate procedures to reduce oil spills and conduct prompt and proper clean up.
**Question for Shell**

What steps is Shell taking to undertake stakeholder outreach? How is Shell engaging with NGOs and community groups, supporters as well as detractors, to make sure relationships are strong?

**Implications beyond Ogoniland**

UNEP calls for the company to fully review and overhaul procedures for oil spill clean up and remediation. In an email to Amnesty International, UNEP stated “since the terrain, operator and regulators are similar in other parts of the Niger Delta, it is a reasonable assumption to make that there may be similar issues in other parts of the Niger Delta.” If this is the case, SPDC may face additional costs for inadequate oil spill clean up across the Niger Delta.

SPDC does not appear to accept UNEP’s findings on the fundamental inadequacy of RENA. SPDC states: “RENA remains a proven and internationally recognised method to remediate spill sites which is widely used in many countries.” The company also states that “The report noted that in a few specific cases in Ogoniland we did not go deep enough in our pre-clean up assessments and this may have impacted the overall effectiveness of remediation in those areas.”

The UNEP report is clear in its dismissal of RENA as an appropriate remediation method in Ogoniland. Its criticisms are not limited to operational failures in specific “pre-clean up assessments.” It states that “the current approach by SPDC to clean up contaminated sites through remediation by enhanced natural attenuation (RENA) should be discontinued.”

**Questions for Shell**

Has SPDC’s remediation techniques in the Niger Delta been reviewed by external technical experts since the publication of the UNEP report? If so, are the findings of that review publicly available?

If not, when can we expect such a review to be undertaken and completed and by whom?

While that review is pending and as oil spills are ongoing in the Delta, what revisions have been made to RENA to address UNEP’s findings?

SPDC confirms that it “will also review a sample of other remediated sites more widely across the Delta to check that adequate remediation has indeed been carried out.”

This is a welcome development given that the systemic failures in clean up identified by UNEP are likely to be replicated in other areas. However it is important that any such review is independent, fully transparent, rigorous, comprehensive, involves a level of technical expertise equivalent to the UNEP team and is subject to independent scientific review.

In its 2011 Annual Report Royal Dutch Shell states that “It has agreed to establish an independent scientific advisory panel to review SPDC practices in the rehabilitation and remediation of oil spill sites in the Niger Delta.” No further details are provided.

**Question for Shell**

Will the company provide the terms of reference for this panel together with information on its members and the processes in place to ensure transparency, independence and credibility for stakeholders?
Adequate oversight by Royal Dutch Shell of its Nigerian subsidiary

SPDC is a subsidiary of Royal Dutch Shell. Given the UNEP report’s findings, questions should be asked about the level of oversight exercised by Royal Dutch Shell of its Nigerian subsidiary. Oil spills remain unacceptably high in the Niger Delta and the clean up failures identified in the report has exposed SPDC to increased clean up costs owing to the worsening of contamination through delay.

Questions for Shell

Is remuneration of middle and senior managers and executives of SPDC in part based on spill reduction in the Niger Delta?

What steps are Royal Dutch Shell taking to ensure the application by SPDC of group environmental standards?

Conclusion

The UNEP report is troubling reading for investors. It presents evidence of systemic failures in SPDC’s oil spill clean up and remediation process. It highlights the potential for significant and previously unconsidered financial liabilities in Ogoniland which may be replicated across SPDC’s Niger Delta operations. Investors should engage with Royal Dutch Shell to determine its plans for addressing the issues identified in the UNEP report both in the short-term and long-term and to seek greater disclosure regarding potential financial liabilities in Shell’s Nigerian operations.
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