

Aurora

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REVIEW OF THE PETROLEUM INDUSTRY ACT, 2021

INSIDE TOLG ADVISORS

INTRODUCTION

On 16 August 2021, the President of the Federal Republic of Nigeria, President Muhammadu Buhari signed the Petroleum Industry Bill, now known as the Petroleum Industry Act, 2021 (the Act) into law. Quite significantly, the new Act seeks to provide legal, governance, regulatory and fiscal framework for the Nigerian petroleum industry and the development of Host Communities, amongst others, with the key objective being to overhaul and transform the Nigerian oil and gas industry.

Structurally, the Act is divided into 5 Chapters, 319 Sections and 8 Schedules.

The Chapters contained in the Act relate to:

- a. Governance and Institutions.
- b. Administration.
- c. Host Communities Development.
- d. Petroleum Industry Fiscal Framework; and
- e. Miscellaneous Provisions,

The 8 Schedules of the Act respectively provide for:

- a. The Minister's rights of preemption of petroleum products in the case of national emergencies.
- b. Incorporated Joint Ventures.
- c. Domestic Base Price and Pricing Framework.
- d. Pricing Formula for Gas Price for the Gas Based Industries.
- e. Capital Allowances.
- f. Production Allowances and Cost Price Ratio Limit.
- g. Petroleum Fees, Rents and Royalty; and
- h. Creation of the Ministry of Petroleum Incorporated.

This publication highlights major provisions in each chapter of the new Act which industry players must now take cognizance of.

A. GOVERNANCE AND INSTITUTIONS

The key objectives of this Chapter are to ensure good governance and accountability, create a profit driven national petroleum company, foster a conducive business environment for petroleum operations, and deepen local content practice in the Nigerian oil and gas industry. It provides for the following key terms:

- a. Vests the ownership of petroleum within Nigeria and its territorial waters, continental shelf and exclusive economic zone in the Government of the Federation of Nigeria.
- b. Retains the Minister's general oversight and supervisory powers in the industry, with regards to formulating, monitoring, and administering policies of the Federal Government for upstream, midstream, and downstream petroleum operations. However, it curtails the previous sole discretion and power of the Minister to grant or revoke oil licenses, with a requirement that the Commission or Authority (as the case may be and as provided below) provide recommendations to the Minister before such approvals/revocations.
- c. Creates a Nigerian Upstream Regulatory Commission ('the Commission'), responsible for the technical and commercial regulation of the upstream petroleum operations, as previously performed by the Department of Petroleum Resources, including with respect to; exploration, development and production activities; elimination of gas flaring, and; the grant of new licenses known as petroleum prospecting licence, petroleum exploration licence and petroleum mining lease, respectively.
- d. Creates the Nigerian Midstream and Downstream Petroleum Regulatory Authority ('the Authority') to be responsible for the technical and commercial regulation of the processing, transportation, transmission and storage of petroleum and gas products (including price) in midstream and downstream operations in Nigeria, such as petroleum liquid operations, domestic natural gas operations and export natural gas operations. to create value over time.
- e. Provides that parties conducting upstream petroleum operations in Nigeria are free to invite the Commission to provide them any assistance that the parties may require. Howbeit, the Commission shall determine on its own, the merits of such requests for assistance.
- f. Provides for the incorporation of a commercial and profit focused Nigerian National Petroleum Corporation Limited (NNPC Ltd) under the Company and Allied Matters Act, 2020 (CAMA) within 6 months from commencement of the new Act, with ownership vested in the Ministry of Finance Incorporated (and Ministry of Petroleum Incorporated) on behalf of the Federation, to take over assets, interests, and liabilities of NNPC. It becomes mandatory for the NNPC Limited to conduct its affairs on a commercial basis and in a profit-efficient manner without recourse to government funds with 20% of its declared profits retained to grow its business.
- g. Provides for the creation of a Frontier Exploration Fund which shall be serviced by 30% of NNPC Limited's profit from any production sharing, profit sharing and risk service contracts. The said Fund shall be for the purpose of exploring and developing frontier acreages, as appropriated by the National Assembly.
- h. Provides for the establishment of a Midstream and Downstream Gas Infrastructure Fund, which shall be funded by 0.5% of the wholesale price of petroleum and gas sold in Nigeria, gas flaring penalties, donations and grants, amongst others, for the purpose of making equity investments of government owned interests in midstream and downstream infrastructures.
- i. Provides that the Commission may impose special terms and conditions for the grant or renewal of a licences/leases. Howbeit, the intention is that such special terms and conditions, as imposed, shall be consistent with the existing provisions of the Act.

B. ADMINISTRATION

The key objective of this Chapter is to promote the exploration and exploitation of petroleum products for the benefit of the Nigerian people upon principles of effectiveness, efficiency, transparency, accountability, competitiveness, conduciveness, and safety, amongst others. It provides for the following key terms:

- a. Administration of acreage for upstream petroleum operations in Nigeria, and adoption of a national grid system for acreage management by the Commission.
- b. Responsibility of the Commission to make recommendations to the Minister with respect to the granting of licences or lease to operating companies incorporated and validly existing in Nigeria under the Companies and Allied Matters Act, 2020.
- c. Introduction of new forms of the major licences/lease to be issued for upstream operations, which are:
 - i. Petroleum Prospecting Licence (PPL, equivalent to the previous Oil Prospecting Licence), which is granted for exploration of Petroleum on an exclusive basis and shall be for a renewable period of 3 years (for onshore and shallow water acreages) and 5 years (for deep offshore and frontier acreages);
 - ii. Petroleum Exploration Licence (PEL, equivalent to the previous Oil Exploration Licence), which is granted for exploration of petroleum on a speculative and non-exclusive basis and shall be for a renewable period of 3 years; and
 - iii. Petroleum Mining Lease (PML, equivalent to the previous Oil Mining Lease), which is granted to a qualified applicant to search for, win, work, carry away and dispose of crude oil, condensates and natural gas and shall be for a renewable period of 20 years. Such license/leases also entitle the holder to rights of way relating to its operations in its respective regard, but subject to the approval of the Commission.



- d. Upon expiration, all existing Oil Prospecting Licenses (OPLs) and Oil Mining Licenses (OMLs) shall be automatically converted to PPLs and PMLs. However, holders of such OPLs and OMLs may voluntarily convert them to PPLs or PMLs, for the purpose of benefiting from the fiscal provisions of the Act. Amongst other conditions, all on-going arbitration and court cases regarding such OPL and OML at the time of such conversion shall be terminated.

e. Existing producing marginal fields shall continue to operate under the original royalty and farm out agreements until their conversions, but shall convert to PML within 18 months from the commencement of the Act. Non-producing marginal fields shall be converted to PPL Licenses.

f. Revocation of licence, lease or permit (as the case may be) due to, amongst others: failure to conduct operations in accordance with international best practices, existing laws (including the Act), or agreed licence/lease terms; interruption of operations for 180 consecutive days without justification; failure to remit required taxes and fees as at when due; transfer of interest without due regulatory consent, Court-ordered bankruptcy, insolvency, or liquidation, failure to comply with regulatory orders, failure to submit a field development plan or comply with environmental laws, or obtainment of license or lease by fraudulent practices or means.

g. Requirement on the Commission to develop a model licence and model lease to include a carried interest provision, giving NNPC Limited the right to participate up to 60% in a contract.

h. Licensee or lessees in upstream petroleum operations must submit for approval an environmental management plan in respect of projects which require environmental impact assessment within one year of the effective date of the Act or six months after the grant of the applicable licence or lease. There is also the requirement for a prescribed financial contribution to an Environmental Remediation Fund established by the Commission, for the rehabilitation or management of negative environmental impacts with respect to the licence or lease.



i. The Authority is responsible for granting, renewing, modifying and extending licences and permits to operators in the midstream and downstream sector. Such rights in the licences and permits cannot be assigned or transferred without the prior written consent of the Authority. Also, where the licence relates to the operation of a refinery, this is issued by the Minister on recommendation by the Authority. The Authority is also empowered to impose public service obligations on licenses and determine the pricing framework for transportation, distribution, and processing of petroleum and natural gas in Nigeria; in a manner that is cost reflective and allows for reasonable return for the operators.



j. A licensee or lessee shall pay a gas flaring penalty prescribed pursuant to regulation issued by the Commission. Such monies shall be utilized for environmental remediation and relief of the host communities impacted. However, gas flaring may be allowed: in the case of an emergency; pursuant to an exemption granted by the Commission, or; as an acceptable safety practice under established regulations. Upstream operators that produce natural gas must therefore submit to the Commission, a natural gas flare elimination and monetisation plan, within 12 months of the effective date of the Act.

k. Requirement for domestic gas supply to be prioritized over exports. Also, crude oil supply obligations shall only be to licensees with operational refineries, on a willing supplier and willing buyer basis.

l. Requirement of licence for processing, storage, distribution, wholesale/retail transportation of gas or petroleum liquid; operation of distribution or aggregation network, supply facility regarding gas or petroleum liquid, as the case may be. Subsisting operators must apply to the Authority for appropriate licenses/permits within 18 months from the passing of the Act.

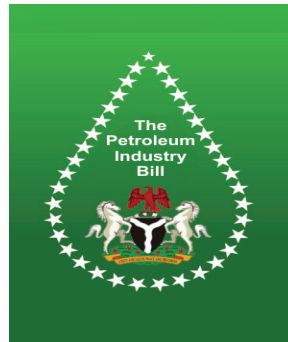
m. Promotion of consultation by the Commission or Authority with stakeholders, in respect of upstream, midstream and downstream petroleum operation regulations, except in a case of national interest or exigency.

n. Requirement of written approvals for decommissioning and abandonment of petroleum wells, installations, pipelines or plants for petroleum operators on land and offshore, some of which must be done in line with good international petroleum industry practice and guidelines issued by the Commission or Authority.

C. HOST COMMUNITIES

The objectives of this chapter are to foster sustainable prosperity within host communities, provide direct social and economic benefits from petroleum operations to host communities, enhance peaceful and harmonious co-existence between licensees or lessees and host communities, and create a framework to support the development of host communities. It provides for the following key terms:

- a. Requirement for settlers to incorporate a Host Community Development Trust (the Trust), within specific time frames, which shall aid the development of the economic and social infrastructure of the communities within the petroleum-producing area. Failure to comply with this requirement may result in the revocation of the applicable licence or lease.
- b. Requirement that settlers conduct a host community needs assessment and develop a Community Development Plan to address the specific needs of each host community. Such needs may relate to infrastructural development, economic empowerment opportunities, educational development, health care, security, or environmental protection issues, amongst others.
- c. The Trust shall be funded by each Settlor with 3% of its actual annual operating expenditure of its preceding financial year, and such funds shall be exempted from tax, with the funds deductible for the purposes of hydrocarbon tax and companies' income tax, as applicable.



D. FISCAL PROVISIONS

The objective of this chapter is to introduce the Petroleum Industry Fiscal Framework (PIFF), which is aimed at encouraging investment in the Nigerian petroleum industry, balancing rewards with risk and enhancing revenues to the Federal Government, providing clear and dynamic fiscal rules of general application, ensuring a fair return for investors, simplifying the administration of petroleum tax, and promoting equity and transparency in the petroleum industry fiscal regime. It provides that:

- a. All money collected from the petroleum industry that are due to the government, inclusive of all taxes, royalties, profit shares, fees, fines, amongst others, are to be timeously transferred to the Federation Account.
- b. The Federal Inland Revenue Service (FIRS) shall assess (in US Dollars) and collect Hydrocarbon Tax of 15% (for converted PPL) and 30% (for converted PML) on profits from oil, condensates, and natural gas liquids production which are from Associated Gas, in the onshore and shallow water from companies engaged in upstream petroleum operations. The Hydrocarbon Tax replaces the previous Petroleum Profits Tax and shall not apply to deep offshore projects to encourage exploratory activities in that area.

c. Tax deductions for expenses that are wholly, reasonably, exclusively and necessarily incurred for matters such as lease/licence rents, paid royalties, repairs of plants and machineries, drilling of first exploration well, drilling of first and second appraisal wells, amounts paid for approved decommissioning and abandonment, or for incurred fees and approved Trusts under the Act, amongst others.

d. Non-allowable deductions for expenses in relation to penalties, gas flare fees, purchase of certain information regarding petroleum deposits, bad debts, loan interests, bank charges, costs for dispute resolution, research and development, production or signature bonuses, custom duties, contributions approved under the Act, amongst others.

e. Assessable profits for any accounting period shall be the amount of the adjusted profit of that period after the deduction of any loss amount from any previous accounting period. Chargeable profits shall be the amount of the assessable profit after allowed deductions.

f. Chargeable Tax for an accounting period shall be 30% of profits from crude oil for PML and 15% of profit from crude oil for PPL

g. Companies Income Tax (CIT) at 30% and Education Tax at 2% are now applicable. The CIT shall apply to companies, concessionaires, licensees, lessees, contractors or subcontractors involved in upstream, midstream and downstream petroleum operations.

h. Allowance of consolidation of costs and taxes for companies engaged in upstream petroleum operations in accordance with the provisions of the Act.

i. Royalties are payable at the rates of 15% for onshore areas, 12.5% for shallow water, 7.5% for deep offshore and frontier basins, and 2.5% to 5% for natural gas. In addition, a price-based royalty ranging from 0% to 10% is payable. The said royalties are to be credited to the Nigerian Sovereign Investment Authority.

j. Late filing of tax returns will attract N10 million on the first day and N2 million for each subsequent day the failure continues. A N20 million fine is applicable to an offense where no penalty is prescribed.

k. Gas utilisation incentive will apply to midstream petroleum operations and large-scale gas utilisation industries. An additional 5-years tax holiday will be granted to investors in gas pipelines.



E. MISCELLANEOUS PROVISIONS

- a. The Act provides its provisions shall prevail in the face of any other inconsistent laws, save for the Nigeria Oil and Gas Industry Content Development Act, and subject to the provisions of the Constitution of the Federal Republic of Nigeria, 1999.
- b. The Act repeals the following Acts:
 - i. Associated Gas Reinjection Act, 1979, CAP A25, Laws of the Federation (LFN) 2004, and its amendments;
 - ii. Hydrocarbon Oil Refineries Act No. 17 of 1965, CAP H5 LFN 2004;
 - iii. Motor Spirits (Returns) Act, CAP M20 LFN 2004;
 - iv. Nigerian National Petroleum Corporation (Projects) Act No. 94 of 1993, CAP N124 LFN 2004;
 - v. Nigerian National Petroleum Corporation Act (NNPC) 1977 No, 33 CAP N123 LFN as amended, when NNPC ceases to exist pursuant to section 54(3) of the Act;
 - vi. Petroleum Products Pricing Regulatory Agency (Establishment) Act 2003;
 - vii. Petroleum Equalisation Fund (Management Board etc.) Act No. 9 of 1975, CAP P11 LFN 2004;
 - viii. Petroleum Equalisation Fund (Management Board, etc.) Act, 1975;
 - ix. Petroleum Profit Tax Act Cap P13 LFN 2004, (PPTA); and
 - x. Deep Offshore and Inland Basin Production Sharing Contract Act (DOIBPSCA), 1993 CAP D3, LFN 2004 and its 2019 amendment.



CONCLUSION

Despite mixed reactions from the public and industry players, the new Act is a welcome development for the Nigerian oil and gas industry as it is progressive step for achieving a robust and well regulated industry. We are hopeful that as the industry continues to evolve, continuous amendments to its provisions will help cater for the rights and interests of all stakeholders, whilst ensuring better economic growth for Nigeria.

We are available to assist you with this and other legal and tax related issues you may have at any time.

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Brains & Hammers Limited -

TOLG Advisors is pleased to officially announce the closing of the N1.5bn Private Debt Note Issuance Exercise by Brains & Hammers Limited.

TOLG Advisors acted as Transaction Counsel on this deal and we are proud to be one of the few law firms in Nigeria to have advised on deals of this nature in 2021.

We congratulate our Enterprise, Projects & Infrastructure Team for a job well done.

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