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AMENDMENT OF NIGERIA'S PRODUCTION SHARING CONTRACT REGIME

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INTRODUCTION

The President of the Federal Republic of Nigeria recently signed into law the Deep Offshore and Inland Basin Production Sharing Contracts (Amendment) Act 2019 (the "Amendment Act"). The Amendment Act modified the erstwhile Deep Offshore and Inland Basin Production Sharing Contracts Decree of 1999 (the "Principal Legislation" or the "Decree").

The amendment appears to have been long overdue in view of the provision of the Principal Legislation that the Decree shall be liable to review when the price of crude oil at any time exceeds $20 per barrel, and also after a period of 15 years from its date of commencement, and every five years thereafter.

A report from Nigeria Extractive Industries Transparency Initiative (NEITI) has revealed that the failure to review the terms of the 1993 production sharing contracts has caused Nigeria a minimum financial loss of about US$16 billion in the space of 10 years (2008-2017).

The amendment therefore comes sequel to calls to review the terms of Nigeria's production sharing contract arrangement in a bid to reflect not only the current realities, but to also introduce a new fiscal regime.

THE AMENDMENTS

1. Royalties

The Amendment Act amends section 5 of the Decree by introducing two modes of calculating royalties-field and price basis.

i. **Field Royalty**: The Decree had previously adopted a graduating scale dependent on water depth to determine the amount of royalty payable. Payment of royalties for operating in areas between 201 to 500 metres water depth was fixed 12%, 501 to 800 metres water depth at 8%, 801 to 1000 metres water depth at 4% and operations in areas in excess of 1000 metres water depth, required no royalty. The Amendment Act has modified this position by introducing a fixed royalty rate of 10% for operations in areas with water depth greater than 200 metres.

   The resultant effect of this provision is that operators in deep offshore areas of between 201 metres water depth to 500 metres water depth who had been subjected to a royalty percentage of 12% in the erstwhile Decree, would enjoy a reduction in the percentage of royalty payable. Conversely, operators in areas in excess of 501 to 800 and 801 to 1000 metres water depth who were required to pay royalty at 8% and 4% respectively, would now pay royalty at an increased flat rate of 10%.

The Amendment Act also fixed the percentage of royalty payable in the frontier/inland basin at 7.5%. This represents a 2.5% reduction on the 10% previously payable under the Decree.

ii. **Price Royalty**: The Decree provides that it shall be subject to review if the price of crude oil at any time exceeds $20 per barrel, real terms, and as such, the share of the Government of the Federation in the additional revenue, shall be adjusted under the production sharing contracts to such extent that they shall become economically beneficial to the Government. This provision has also been amended to allow for royalty flexibility in line with the changing prices of crude oil. Therefore, 2.5% royalty shall be payable when the price of crude oil is between US$20 and US$60, 4% between US$60 and US$100, 8% between US$100 and US$150, and 10% for a crude oil price of US$150 and above.

2. Review of Production Sharing Contracts

The Amendment Act also introduces a new section to the Principal Legislation by mandating that the Minister of Petroleum shall cause the Corporation (defined in the Principal Legislation as the Nigerian National Petroleum Corporation) to call for a review of production sharing contracts every eight years. This is a substantial improvement on the Decree which only provides that the provisions of the Decree shall be liable to review after a period of 15 years from the date of commencement and every 5 years thereafter. The objective is to keep the production sharing contracts always commercially viable for the Government.

3. Imposition of Penalty

A penalty section has been introduced by the Amendment Act by providing that any person who fails to comply with any obligation imposed by any provision of the Act shall be liable on conviction, to a fine not below ₦500,000,000 or to imprisonment for a period of not less than 5 years or both.

CONCLUSION

It is apparent that the two modes of calculating royalties-the field and price modes-would occasion an increase in the amount of royalty payable in the industry. Whilst it may be argued that this might deter investments in the sector, this move is aimed at driving an increase in the revenue generated by the Government.

Contributors

Taiwo Adeshina
Terry Akaluzia

Key Contacts

Taiwo Adeshina
Partner
e: taiwoadeshina@jacksonettiandedu.com

Terry Akaluzia
Associate
e: terryakaluzia@jacksonettiandedu.com

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Jackson, Etti & Edu

RCO Court 3-5, Sinari Daranijo Street,
Victoria Island, Lagos, Nigeria.

t: +234 (1) 4626841/3, +234 (1) 2806989 f: +234 (1) 2716889
e: jacksonettiedu@jacksonettiandedu.com www.jacksonettiandedu.com