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KEY ELEMENTS OF THE 2017 NATIONAL PETROLEUM POLICY

At its weekly meeting, held on July 19, 2017, the Federal Executive Council (“**FEC**”) approved a new **National Petroleum Policy (“NPP”)** for the country. The NPP sets a long-term agenda for Nigeria “*to become a nation where hydrocarbons are used as a fuel for national economic growth and not simply as a source of income*”, and sets strategic policy objectives for each part of the petroleum industry and the entire value chain. This long-term vision had previously been articulated in the Ministry of Petroleum Resources’ (“**MPR**”) *7 Big Wins Initiative* and the Federal Government of Nigeria’s (“**FGN**”) *Economic Recovery & Growth Plan (ERGP 2017 – 2020)*.

The NPP, which is expected to be implemented alongside a complementary National Gas Policy (issued one month earlier) and a National Petroleum Fiscal Policy (soon to be finalized), specifically provides for the legal & regulatory, institutional, commercial, fiscal and operational framework for developing a stable and enabling oil and gas landscape in which there will be improved transparency, efficiency, cost effectiveness, attractive investment climate, and a well-protected and sustainable environment.

Set out below are some of the key elements of the NPP:

PRIMARY OBJECTIVES

The primary objectives of the NPP are strategically set with a view to achieving the following:

- Creation of a market-driven oil and gas industry through effective funding of the National Oil Company, encouragement of private investment across the upstream, midstream and downstream segments of the value chain, as well as the separation and clarification of the roles of the state as a policy maker, regulator and investor;
- Maximization of the production and processing of hydrocarbons;
- A departure from the concept of oil as a source of income to oil as a fuel for economic growth;
- Value creation through processing of oil into significant end products for industries, by employing diversification and backward integration strategies to achieve competitive supply of petroleum products, active refining, value added extraction and industrialization;
- the hydrocarbon molecule from extraction to destination markets (this will be facilitated by securing primary and secondary markets outside Nigeria through collaborative ventures with third parties);
- Incentivizing investments in cost-efficient storage, transportation and distribution system for petroleum products in Nigeria (through effective management of supply and distribution interruptions as well as ending discriminatory practices in regulation and access to midstream infrastructure);
- Promotion of competition in the petroleum industry;



- Minimizing the environmental footprint of oil exploration in Nigeria (through strict enforcement of environmental laws); and
- Managing the balance between depleting oil resources and renewable energy.

POLICY INITIATIVES

The above policy objectives of the NPP are addressed under a number of policy areas, including:

1. Governance

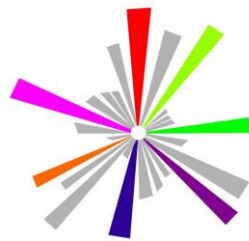
This covers the legal and regulatory, institutional, commercial, fiscal and sector financing framework for the petroleum industry, as well as provisions for sovereign wealth fund and Niger Delta development. The critical reforms expected to be driven by the whole governance architecture are hereunder highlighted:

- Promotion of new legislation, unbundling of the NNPC and establishment of new entities

The FGN intends to promote the enactment of new legislation, including the Petroleum Industry Reform Bill (“**PIRB**”), which will form the **legal and regulatory framework** for addressing a broad range of issues, including sector governance, fiscal regime, transparency and accountability, and environmental sustainability among others.

Also, new entities are proposed to be established, pursuant to the PIRB, including:

- (i) National Petroleum Policy Directorate (“**Directorate**”) within the MPR – to act as a technical ‘Back Office’ for assisting the Minister of Petroleum Resources (“**Minister**”) in the formulation, monitoring and ensuring implementation of petroleum policies;
- (ii) Nigerian Petroleum Regulatory Commission (“**Commission**”) – which will be a new, independent, single regulatory body responsible for the technical and economic regulation of the entire petroleum sector;
- (iii) National Oil Company of Nigeria (“**NOCN**”) – an incorporated public entity to replace the Nigerian National Petroleum Corporation (“**NNPC**”) which will manage certain petroleum assets of the FGN, with equity to be listed on local and international markets;
- (iv) National Petroleum Asset Management Corporation (“**NPAMC**”), which will manage other petroleum assets of the FGN which are not allocated to the NOCN;



BANWO & IGHODALO

- (v) Investment Promotion Office (“IPO”), which will be one of the divisions within the MPR and which will work in conjunction with the Nigeria Investment Promotion Council (“NIPC”) in order to facilitate investments in the Nigerian petroleum industry.

- **Streamlining of policies and full legal separation of operations across the value chain**

The NPP also provides for a robust **institutional framework** for ensuring smooth and seamless operations along the petroleum industry value chain. First, the NPP proposes the establishment of the Commission as a single regulator for the whole petroleum sector (thereby replacing all existing regulatory entities) in order to address challenges of information gaps among multifarious regulatory entities, over-regulation, regulatory overlaps and lacunae. Specific regulatory issues proposed to be within the Commission’s remit include: (i) upstream oil and gas licensing (ii) midstream licensing and economic regulation (iii) downstream petroleum products licensing and regulation (iv) downstream gas licensing and regulation (v) health and safety compliance (vi) environmental compliance (vii) consumer protection (viii) metering and measurement (ix) cost monitoring & control (x) inspection, investigation and compliance monitoring, and (ix) developing technical standards working with industry stakeholders. Although the Commission is proposed to exist independently of the MPR, its operations are expected to be in line with the MPR’s policy directions.

Also, it is expected that clear and distinct regimes for different operations across the value chain will be promoted, such that there is full legal separation between the upstream, midstream and downstream segments of the petroleum industry.

- **Full legal separation of infrastructure ownership and operations, and trading**

The NPP proposes a **commercial framework** for opening up access to pipelines and networks as well as setting pricing principles and regulations for the petroleum industry.

First, this initiative is to ensure that the different activities of infrastructure ownership, operations, and trading in the petroleum industry are carried out by separate companies. Whilst asset owners in one segment of the value chain may own and operate assets in different segments of the value chain if they wish to do, they will only be able to do this via separate corporate vehicles. In other words, a group of companies may comprise of a holding company having interests in different legal entities operating in the upstream, midstream and downstream segments.

Second, the initiative promotes the introduction of a suitable and effective network code to govern open access to all pipelines and other essential midstream infrastructure, located either offshore or onshore.



Third, the initiative will promote the adoption of “cost-of-service approach” in the sector, using average, standard or benchmark costs. Essentially, a regulated tariff regime will be introduced for the monopoly infrastructure areas of the industry, in a manner that will provide investors the opportunity to recover all eligible costs with reasonable return on investment.

- **Separate fiscal regime each for Oil and Gas**

The NPP envisions a new **fiscal framework** that will separate oil from gas. In essence, gas projects will be developed based on their economics and not dependent on, or consolidated against, oil taxation.

Currently, it is permissible under the *Associated Gas Framework Agreement (“AGFA”)*, for Associated Gas (AG) and Non-Associated Gas (NAG) costs to be recovered from oil income through cross-subsidizing of oil projects to gas projects. This new fiscal framework seeks to eradicate the distortions in the AGFA by emplacing a corrective and optimum fiscal regime tagged *Fiscal Rules of General Application (“FRGA”)*. Whilst the FRGA is good for the development of the gas sector and the overall petroleum industry, we note that the AGFA (which it seeks to repeal) is codified in sections 11 and 12 of the Petroleum Profits Tax Act. Consequently, the NPP-birthed FRGA may not become effective in enforcing the desired separate oil and gas tax regimes until the PIRB or any other legislation is passed into law in order to implement the FRGA.

- **Financing mechanisms for the petroleum sector**

The NPP is expected to encourage **sector financing**, in a manner that will encourage all types of project financing mechanisms with minimal role for the Government in the future. In essence, project financing in the sector will be done through one or more of several finance sources including government budget; equity funding by private sector companies or government owned corporations; loans from Nigerian and international commercial banks; and International Financial Institutions (IFIs) including the World Bank, International Financial Corporation and African Development Bank.

There will also be a shift in the use of Joint Ventures (JVs) to the use of Incorporated Joint Ventures (IJVs) and Production Sharing Contracts (PSCs), with the goal of exiting all cash call arrangements under the NNPC JVs (which have proven problematic in the past) by the end of 2017.

- **Sovereign Wealth Fund**

Under the NPP, the Government will explore mechanisms by which petroleum revenues can be used both for financing infrastructure projects and managed for the benefit of future generations. It is therefore intentioned that the Government will agree a cap on the



proportion of petroleum revenues that can be spent on current national expenditure while the remainder will be set aside for funding major infrastructure projects and invested in a Sovereign Wealth Fund (SWF) for future generations.

- **Niger Delta**

The intention of the Government to develop a Niger Delta wide model, which will involve Niger Delta communities directly in infrastructure, social and petroleum development, is well articulated in the NPP. Concepts to be considered include: development of small and marginal fields in partnership with local communities, models for community based trust funds, and small equity holdings for communities with oil operations in their areas. The NPP notes that although the Government intends to take measures to restore long term stability to the region, operators are expected to take the necessary measures to secure their facilities, in the meantime.

2. **Industry Structure and Operations**

The NPP envisages a petroleum industry that will be driven by partnership between the public and private sectors with clear separation of roles between the government sector and the private sector. This is intended to facilitate a new **Industry Structure** with a clean break from the past and one where the private sector is allowed open access to operate and build the market while the Government concentrates on developing and implementing incentivizing and non-discriminatory policies, legislation and regulations, and will only participate through the **corporatization** of state-owned enterprises. To achieve this, the new policy proposes the unbundling of the NNPC and its replacement with the NOCN as a corporatized legal entity to be run in accordance with good corporate governance codes applicable to private companies. The NOCN will: (i) be responsible for managing the FGN's interest in JVs, PSCs and other upstream, midstream and downstream projects (ii) be treated on an equal basis with private sector operators (iii) not be subjected to the FGN's appropriation cycle (iv) have a capital structure which enables asset based financing, combines tax efficiency and financial flexibility, and minimizes financial and business risks, and (v) develop a dividend payment and earnings retention policy in order to ensure predictability of its returns to the FGN. The purpose of the envisaged new structure is to create in Nigeria a market-driven oil and gas industry, structured to meet the vision of a nation where hydrocarbons are used as a fuel for economic growth and not simply as a source of income.

Also intended in the NPP is the **development of resources, infrastructure and markets in the upstream, midstream and downstream operations** in the petroleum industry. The NPP intends to encourage an environment that ensures deliberate exploration and production in other regions of Nigeria, outside the Niger Delta provided it is commercially viable. In furtherance of this, promotion of upstream development activity in inland and offshore basins is intended, including the review of the commercial terms upon which titles in inland basis are held.

It is also envisaged that the **allocation of all petroleum blocks, licences, leases, licence renewals and licence extensions** will be done following a transparent competitive process that



allows local community participation through local community vehicles. Licence renewals or extensions is intended to be based on licence holders making progress in meeting their exploration or production targets, gas flare down and gas supply obligations. As an indication of its commitment to develop the domestic petroleum industry, the Government is expected to continue with the policy of **marginal field awards** to indigenous players.

Also, it is expected that measures will be taken to minimize environmental damage and the **environmental footprint** in the Niger Delta. The NPP proposes the “**name and shame**” strategy (by which details of pollution and the polluters will be published in international media) and the “**polluter pays**” principle (under which polluters pay the full costs of mitigating any damage to the environment or communities). The Government will also consider moving to a system of independent assessment of the environmental and human costs of an oil spill, and may introduce an outright ban on the usual private arrangements involving nominal financial settlement with local chiefs in affected communities.

The NPP also envisions the balancing of petroleum resources utilization within the context of **Renewable Energy**. It is therefore intended that renewable energy will form a significant part of Nigeria’s diversified energy mix especially as the cost of renewable energy continues to decline with renewables gaining ground worldwide. Besides, the long-term future for Nigeria is seen to be in gas and an oil-based petrochemical industry. It is envisaged, in the medium to long term, that gas will be diverted from the power sector and be increasingly used for gas-based industrial purposes. Similarly, oil exports will become proportionately less and less important for the Nigerian economy, as oil refining and oil-based industrialization becomes an integral part of the new industrial economy.

In line with the vision of a **strong refining sub-sector**, the NNPC refineries are expected to become autonomous profit centres, with responsibility for their own commercial operations. Storage depots and ancillary facilities which were hitherto transferred to the Nigerian Pipeline & Storage Company Limited (“**NPSC**”), formerly Petroleum Products Marketing Company Limited (“**PPMC**”), are intended to be returned to the refineries. In their new independent status, the refineries will be given autonomy to source crude oil and sell refined products, as they deem fit. In addition, each refinery will be given a transition period, within which to become commercially viable, failing which non-performing refineries will be divested, concessioned, or closed down. Strategic partnerships, concessions, co-location of new refineries within the precincts of the existing refineries, and other viable structures are being considered, to attract international finance, as well as technical and commercial expertise into NNPC refineries.

The Government intends to also encourage the construction of private refineries as well as invite private sector players to invest in the **construction of midstream and downstream infrastructure**, especially transportation pipelines and facilities for refining, storage and distribution. There is consideration for **economic regulation of jetties in a deregulated environment** to prevent monopoly or oligopoly tendencies that may affect the free flow of refined petroleum products. At any rate, onshore strategic reserves of refined petroleum products will be developed to mitigate the risk of significant disruptions in supply from existing sources, or transportation routes



such as transport jetties at Apapa or Calabar, or commercial arrangements at the terminals affecting the optimal flow of products or pricing. In order to diversify and hence reduce these risks, the government will also investigate the opportunities for increases in jetty capacity in addition to the construction of new jetties.

Petroleum product **pricing is intended to be market-led and end user prices expected to be unregulated** as envisaged in the NPP. However, to avoid information asymmetry and arbitrage, end user prices will be published and prices will be monitored. Further, it is intended that all subsidies will be eventually permanently removed. A transitional arrangement to a fully price-deregulated product market is intended to be developed and implemented.

3. Local Content and Communications

The NPP advocates the building of in-country capacity in the petroleum industry through development of **national human resources** capable of taking a full role in managing the resources within the Nigerian oil and gas sector. It is intended that full compliance with the provisions of the Nigerian Oil and Gas Industry Content Development Act, 2010 ("**Local Content Act**") coupled with qualitative national education and training will be diligently pursued, so as to engender the acquisition by Nigerians of the requisite leadership, management, engineering, and technical skills for operations along the petroleum industry value chain.

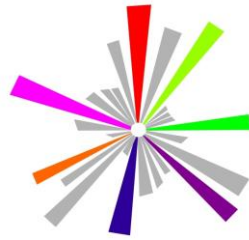
An effective **communications strategy** is proposed in the NPP to be developed as a means of explaining to all stakeholders the purpose of the petroleum policy, and the thinking and analysis behind it. There exists a gulf and lack of understanding between investors and government of their respective expectations and obligations under the new vision of transforming Nigeria from being an oil enclave into a gas-based industrial hub. A two-channel strategy of **internal and external communications** is therefore proposed. The NPP will be explained within the MPR and all government ministries, departments and agencies (MDAs) through the internal communications channel while the external communications channel will be employed in explaining the policy to, and consulting with, industry stakeholders including international investors; domestic investors; civil society; donor community; and the general public.

CONCLUDING REMARKS

Notwithstanding the laudable reforms envisaged by the NPP, industry reaction is likely to be one of cautious optimism, since the policy has emerged in the wake of a crash in crude oil prices and a general migration from dependence on fossil fuels towards renewable energy sources, on the international scene.

For the theoretical agenda and benefits of the NPP to be effectively realised, certain practical steps must be timeously taken. For instance, the National Assembly's enactment of the PIRB into law is critical in order to provide the necessary legislative backing for the objectives of the NPP.

Also, whilst it is commendable that critical policy milestones are set in the NPP, under the roadmap for action within the short term (one year and below), medium term (one to two years), and the long term (two



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years and above); we note that the timelines set for attainment of the specific objectives should be considered sacrosanct so as to engender investor confidence in the entire process. To facilitate this, we advocate periodic review of progress made in the implementation of the NPP, in addition to other practical demonstrations of commitment on the part of Government to attainment of the objectives of the policy.

The Grey Matter Concept is an initiative of the law firm, Banwo & Ighodalo

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