

LEGAL FRAMEWORK AND FISCAL REGIME

Introduction

The ownership and control of all minerals, mineral oil and natural gas in, under or upon any land in Nigeria, its territorial waters and exclusive economic zone is vested in the Federal Government based on the provision of section 44(3) of the 1999 Constitution of the Federal Republic of Nigeria. The Federal Government is mandated to manage such minerals in a manner as may be prescribed by the National Assembly¹.

The Petroleum Act of 1969 is the primary legislation governing petroleum activities in Nigeria. It provides comprehensive provisions for exploration, production and transportation activities in the sector. The Act, like the constitution, vests ownership of petroleum resources on the Federal Government of Nigeria. There are a myriad of other laws and subsidiary pieces of inter-related legislations that deal with specific operations of the industry. The sections of this Act are listed below;

- Vesting of petroleum in the State
- Oil exploration licenses, oil prospecting licenses and oil mining licenses
- Refineries
- Control of petroleum products
- Offences in connection with the distribution of petroleum products
- Price control
- Rights of pre-emption
- Power and duties of public officers
- Regulations
- Discharge of obligation to make payments
- Settlement of duties by arbitration
- Delegation of powers
- Offences

¹ [The 1999 Constitution of the Federal Republic of Nigeria](#)

- Repeals, amendments, transitional and savings provisions
- Interpretation
- Short title and commencement

The fiscal regime in the industry includes those set of laws, regulations and agreements that determine the economic benefits derived by the Government from exploration and production activities.

Other key legislations relating to the sector are listed below;

- Petroleum Profit Tax Act (PPT) 1959, and its amendments
- Regulation 42 of the Petroleum (Drilling and Production) Regulations, 1969
- Petroleum (Drilling and Production) Regulations, 1969
- Petroleum Refining Regulation, 1974
- Associated Gas Re-Injection Act, 1979 & 1985
- Associated Gas Re-injection (Continued Flaring of Gas) Regulations, 1984
- Company Income Tax Act CAP. 60 LFN of 1990
- The Nigerian LNG Fiscal Incentives, Guarantees and Assurances CAP N87, 1990
- Associated Gas Framework Agreement (AGFA) 1991 & 1992
- The Petroleum (Drilling and Production) regulations Act No. 69 LFN of 1996
- Deep Offshore and Inland Basin Production Sharing Contracts Act (No. 9) of 1999
- GAS Finance (Miscellaneous Taxation Provisions) Acts 18 & 19 of 1998 and Act 30 of 1999
- Memorandum of Understanding (MOU) (2000) between the Federal Republic of Nigeria, Nigeria National Petroleum Corporation and all JV companies
- Deep Water Block Allocations to Companies (Back in Rights) Regulations (2003)
- Oil Prospecting License (conversion to Oil Mining Leases) Regulations
- Petroleum Act (2004) Cap. (P10), LFN
- Associated Gas Re-Injection Act (2004) Cap (20), LFN
- Petroleum Profits Tax Act (2004) Cap (P13), LFN
- Oil Pipelines Act (2004) Cap. (07), LFN
- Hydrocarbon Oil Refineries Act (2004) Cap (H5), LFN

- Petroleum Act of 1969 as amended by Cap 10 Volume 13 Law of Federation of Nigeria (LFN) 2004
- Marginal Field Operations (Fiscal Regime) Regulations 2005
- Companies Income Tax Act Amendment (Section 39) 2007
- National Domestic Gas Supply and Pricing Regulations 2008
- Nigerian Oil & Gas Industry Content Development Act 2010 (the NCDA)

These legislations and regulations govern various aspects of operations in the Industry including how businesses should be formed and organized. Others describe the operating standards for all operators, their scope of operation and their responsibility to the government, environment, host communities and the international community. Some of the laws also create agencies that implement government policy and ensure compliance with the respective enabling laws.

Fiscal terms

Find below a summary description of fiscal terms governing the industry;

Petroleum Profit Tax

The Petroleum Profit Tax Act (PPTA) is the tax law that governs the taxation of companies engaged in petroleum operations. The Act defines petroleum operations as “the winning or obtaining and transportation of petroleum or chargeable oil in Nigeria by or on behalf of a company for its own account by any drilling, mining, extracting or other like operations or process, not including refining at a refinery, in the course of a business carried by the company engaged in such operations, and all operations incidental there to and sale of or any disposal of chargeable oil by or

on behalf of the company”². PPT payments are made either in cash or in-kind depending on the operating contract of the company.

The PPTA provides for the determination of assessable tax, chargeable tax and the recovery of tax. Variable taxes are applicable for the different terrains as follows;

a) Terrain Onshore/Shallow offshore

First five years (producing companies)	85%
First five years (new comers)	65.75%
Subsequent years (all companies)	85%

All percentages above are of chargeable profits for that period.

b) For deep offshore

- i. The PPTA provides that the PSCs which executed a contract in 1993, shall during the duration of the PSC be entitled to claim an investment tax credit allowance as an offset against tax of 50% (of chargeable profit) in accordance with the provisions of the PSC

The Deep Offshore Inland Basin Decree provides further that;

- ii. The PPT applicable to a contract area in a PSC shall be 50 flat of chargeable profits for the duration of the PSC
- iii. In respect of parties who executed PSCs after 1st July 1998, provides for an investment tax allowance at a flat rate of 50% for capital expenditure incurred wholly for the purposes of petroleum operations in the accounting period for which the asset was first used

²www.firs.gov.ng/Tax-Management/Tax%20Legislations/PPTA.pdf

Royalty on oil

Royalty refers to payments, either in cash or in kind, made by a holder of a concession to the Federation based on the value of the quantity of crude oil produced (saved after the oil has been separated from its components) from the field within the concession area in line with the fiscal terms approved statutorily by the Government.

Royalty payment is a statutory obligation of every corporate body involved in the production of oil and gas. It is guided principally by the Petroleum Act of 1969 as amended by Cap 10 Volume 13 Law of Federation of Nigeria (LFN) 2004. The Petroleum (Drilling and Production) regulations Act No. 69 LFN of 1996 Section 60 stipulates that royalty on crude oil and casing head petroleum spirit is computed by applying the appropriate rate of royalty to the chargeable value of crude oil and casing head petroleum spirit under the regulation. Calculation of chargeable oil as provided in the 1996 regulation Act is as follows;

- a) ascertaining the quantity of crude oil produced on a field by field basis in the relevant OML; and
- b) reducing that quantity by the deduction of;
 - Quantities used for production operations
 - Quantities used for re-injection
 - Quantities lost through evaporation

The Act (section 63) also explains that "casing-head petroleum spirit" means any liquid hydrocarbons which;

- c) have been obtained from natural gas by natural separation or by any chemical or physical process; and
- d) have not been refined or otherwise treated.

From the above it can be inferred that royalty is calculated on net crude oil produced on a field by field basis. NEITI Report 2013³ comments that DPR interprets this to mean that royalty is assessed on net crude oil production after removal of associated gas, water, sediments and other impurities.

The calculation and payment of royalty on oil is guided by Section 61 of the 1969 Petroleum Act as amended.

$$\text{Royalty (R)} = V * P * R$$

Where: R	Royalty rate (depending on the terms and terrain)
V	Production volume
P (Crude oil price)	NFP ⁴ as adjusted by API gravity of the crude oil

The Royalty rates for crude oil are;

a) Onshore areas	20%
b) Offshore areas	
○ Areas up to 100m water depth	18.5%
○ Areas up to 200m water depth	16.5%
○ Areas from 201 to 500m water depth	12.5%
○ Areas from 501 to 800m water depth	8%
○ Areas from 801 to 1000m water depth	4%
○ Areas beyond 1000m water depth	0%

³ <http://neiti.gov.ng/index.php/neiti-audits/oil-and-gas/category/161-2013-audit-report>

⁴ New Fiscal Price for the computation of royalty oil and PPT

Royalty on gas

Royalty on gas is based on gas sales and refers to the sum paid by the holder of a Concession to the Federation based on the volume of gas produced and sold from the fields within the concession in line with the following fiscal terms:

- | | |
|-------------------|----|
| a) Onshore Areas | 7% |
| b) Offshore Areas | 5% |

Determination of price for the computation of royalty for oil and PPT

In practice, Price used in the computation of royalty for oil and PPT has been in contention since the termination of the 2000 Memorandum of Understanding (MOU)⁵ in 2007. While the government provided for the use of Official Selling Price (OSP), companies used the Realisable Price (RP) for computations. Negotiations between OPTS (for companies) and DPR (for government) has led to a consensus. DPR has directed all operating companies to comply with the NFP effective January 2015 while joint venture companies are to adopt the NFP effective July 2010. The NFP will adopt three⁶ international benchmarks for its computation.

Company Income Tax

Company Income Tax is tax paid on profit arising from gas operations of companies. Oil and Gas companies pay Company Income Tax in United States Dollar, on profit arising from gas operations.

⁵ Memorandum of Understanding (MOU) (2000) between the Federal Republic of Nigeria, Nigeria National Petroleum Corporation and all JV companies

⁶ PLATTS, ARGUS and ICIS-LOR