THE PIA'S SOLUTION FOR PROSPECTING LICENCE HOLDERS:

South Atlantic Petroleum Limited V. Minister of Petroleum Resources & Ors Reviewed

Introduction

Laws should ideally not apply retrospectively, but in some cases where a new law closes an important gap in the regulatory regime, there is a temptation to wish that that the law retrospectively applies to amend the injustices of the past. An example is the Petroleum Industry Act, 2021 (PIA) and the rights of prospecting licensees to take full advantage of their petroleum discoveries.

The case of *South Atlantic Petroleum Limited (SAPETRO) V. Minister of Petroleum Resources & Ors*[1] (the "*SAPETRO Matter*") spotlights the less-than-ideal predicament of prospecting licensees under the Petroleum Act, 1969 (Petroleum Act), as it pertains to conversion of prospecting licences to mining leases. Using the Sapetro Matter as a backdrop, this article explains how the provisions of the PIA now provide more explicit direction and certainty to prospecting licensees, to facilitate the transition of their field operations from the prospecting phase to the mining phase.

The SAPETRO Matter

In 2005, 16 years before the PIA was enacted, SAPETRO was unjustly prevented from taking full value of half of its Oil Prospecting Licence (OPL) 246 (500 sq. miles). OPL 246 consisted of 1000 sq. miles when it was awarded to SAPETRO in 1998 for 5 years (renewed in 2002 for another tenure of 5 years); SAPETRO had discovered oil in commercial quantities in the eastern half of the OPL (500 sq. miles) and proceeded to apply to the Minister of Petroleum Resources (the "**Minister**") for conversion of the eastern half to an Oil Mining Lease (OML) under the Petroleum Act. The Federal Government approved

[1] *(2023) 7 NWLR (Pt. 1882) 135*

the application and granted the OML 130 lease over the eastern half, which is where you currently have the prolific Egina and Apo fields that have to date produced close to a billion barrels of petroleum.

What do you think happened to the remaining western half of OPL 246? SAPETRO was in fact denied the opportunity to convert the western half to an OML on the basis of a government policy that one half of an OPL should be relinquished back to the government irrespective of whatever prospects still exists in the OPL. We can assume that the significance of this was SAPETRO losing the opportunity to unlock potentially another 1 billion barrels of petroleum production. As you can imagine, Sapetro sued to protect its claim to the western half after its application to convert it to an OML was denied by the Minister.

The Courts' Decisions

At the conclusion of trial brought by way of a judicial review, the trial court dismissed SAPETRO's claim and held, in the main, as follows:

- SAPETRO was not entitled to a mandatory grant of an OML over the remaining portion of OPL 246 (western half);
- the Minister has the discretion whether or not to grant an additional OML to SAPETRO from the remaining portion of OPL 246 and is not under any legal duty to give reasons for refusing to grant an additional OML;
- there is nothing unlawful in the government policy that the remaining portion of OPL 246 after the grant of OML 130 to SAPETRO, automatically relinquishes and reverts to the Federal Government.

This decision by the trial court was to reinforce the government policy that was presumably not communicated to SAPETRO when it was granted the licence over all the areas covered by OPL 246 and made investments to discover petroleum prospects on both the eastern and western halves. The court sided with the government to punish SAPETRO for succeeding in the eastern half and denying it the opportunity to replicate the success in the western half.

As you would imagine, SAPETRO was dissatisfied with the decision of the trial court and appealed to the Court of Appeal. While the appeal was pending, OPL 246 expired in 2008 by effluxion of time and the court dismissed the appeal for becoming academic. SAPETRO appealed unsuccessfully to the Supreme Court, but the outcome was the same as the Supreme Court upheld the Court of Appeal's decision.

The SAPETRO Matter is a good example of how prospecting licensees were disenfranchised by arbitrary government policies premised on the misapplication of the Petroleum Act to the process of converting OPL discoveries and prospects into mining assets.

The Prospecting Licensee's Predicament Under the Petroleum Act and the PIA's Innovative Solutions

For more context, an OPL is granted pursuant to paragraph 5 of the First Schedule to the Petroleum Act, 1969, and confers the holder with the exclusive right to explore and prospect for petroleum within the area of the licence. The ultimate objective of the OPL is to discover petroleum and proceed to mine it for sale. If a licensee makes a discovery, the OPL is then converted to an OML by virtue of paragraph 8 of the First Schedule to the Petroleum Act, 1969:

> *"An oil mining lease **may be granted** only to the holder of an oil prospecting licence who has –*
> *(a) satisfied all the conditions imposed on the licence or otherwise imposed on him by this Act; and*
> *(b) discovered oil in commercial quantities."* (emphasis ours)

Unfortunately, the above wording of the Petroleum Act is not very helpful in protecting the rights of a licensee in this situation, which as we saw in the SAPETRO Matter led to a significant loss of value. The PIA does much better in this regard and effectively improves the regulatory environment in the following key ways:

1. **Removal of Administrative Discretion in the Approval of License Conversion Applications**: The use of the word "*may*" in the above provision gives the Minister a discretion in approving an application for conversion of an OPL to OML. This discretion presents a huge risk to investors and to security of title because even if the OPL holder has fulfilled all the requisite conditions for grant of an OML the Minister could decide not to grant the application to convert the OPL to an OML without the need to state any reasons whatsoever. The SAPETRO Matter shows that this risk is real, as the court held that the Minister could deny conversion of an OPL to OML and not be required to give any reason.

   Unlike the Petroleum Act, Section 81(1) of the PIA – provides that:

   > "*A petroleum mining lease **shall be granted** for each commercial discovery of crude oil* or *natural gas or both, to the licensee of a petroleum prospecting licence who has*;
   > *(a) satisfied the conditions imposed on the licence or the licensee under this act;*
   > *(b) received approval for the applicable field development plan from the Commission* (emphasis ours).

   The use of "shall" in the PIA instead of "may" as used in the equivalent provision of the Petroleum Act, is deliberate and indicates the intendment of the legislature to ensure that PPL holders have more certainty around the conversion from prospecting to mining phases. The above provision effectively removes administrative discretion and clearly entitles a licensee, who has fulfilled the listed conditions, to convert his Petroleum Prospecting Licence (PPL) to a Petroleum Mining Lease (PML).

2. **Retention – More Options for OPL holders**: The above provision of the Petroleum Act also increased the risk profile for investments in OPLs, by requiring that the only outcome of its exploration activities was to find oil in commercial quantities (10,000 barrels of oil per day). Like most businesses, an OPL holder will typically only proceed to develop any discovery if the expected production will generate enough revenues (based on the oil price forecast) to payback the investment ("commerciality"). This 10,000-barrel threshold does not correctly track commerciality. Other factors missing from this picture are the oil price, terrain, development costs and potential for an optimised development with another field. The Petroleum Act unfortunately, does not give the OPL holder another option if it cannot justify commercial

quantities immediately and this jeopardises all historical investments in the field, which was the experience of SAPETRO with respect to the remaining portion of OPL 246.

One way the PIA addresses this issue is by introducing the term commercial discovery (in place of "commercial quantities") which it defines as a discovery that "…can be economically developed in the opinion of the licensee or lessee after consideration of all relevant economic factors normally applied for the evaluation and development of crude oil, natural gas or condensate"[2]. This definition better reflects the factors the licensee must consider in determining the commerciality of a discovery.

The more impressive innovation of the PIA is that it introduces the concept of retention which entails that when a PPL holder makes a discovery in the licence area and is unable to immediately declare such a discovery to be a commercial discovery, it can declare a significant oil or gas discovery- which entitles it to retain the discovery for a period of not more than 10 years (i.e. retention period).[3] The PIA defines a significant discovery as a discovery that is substantial in terms of reserves and is potentially commercial, but cannot be declared commercial for reasons which include lack of markets or infrastructure.[4]

Note that this retention period elongates the duration of the PPL in respect of the retention area and the licensee is able to conduct further exploration and appraisal activities on the field, towards elevating its status to a commercial discovery worthy of conversion to a mining lease.

By providing more options for the PPL holder, the PIA has also removed the anomaly that previously existed in the industry, whereby OPLs were being renewed beyond the limit set by the Petroleum Act, [5] perhaps because in such cases, it seemed unfair to take away the discoveries made by a licensee abruptly, given the amount of investments made to achieve the discovery.

3. **Clarity on relinquishment and status of unconverted portions of an OPL**: The Petroleum Act does not contain any provisions on relinquishment of licence areas for OPLs and is also silent on the status of the remainder of an OPL upon conversion of a portion of the OPL to an OML. The Oil Prospecting Licences (Conversion to Oil Mining Leases, etc.) Regulations, 2004 (the "**Regulations**") made pursuant to the Petroleum Act does not address the issue of relinquishment. This begs the question why the court upheld a government policy over a right granted by statute.[6]

   Although the Regulations provide for the grant of more than one OML from an OPL area, they do not expressly provide for the subsistence of the OPL holder's rights to see out the unconverted portion of the OPL after the grant of an OML. It is this vacuum that the unfair government policy canvassed in the SAPETRO Matter exploited, to deny SAPETRO its right to the unconverted portion of OPL 246.

[2] *Section 318 of the PIA*

[3] *Section 78(9) & (10) of the PIA*

[4] *Section 318 of the PIA*

[5] *Paragraph 6 of the Second Schedule to the Petroleum Act*

[6] *Section 44 (1) of the 1999 Constitution of the Federal Republic of Nigeria prohibits the compulsory acquisition of immovable property except in the manner and for the purposes prescribed by a law. See also Elf Pet. (Nig.) Limited v. Umah (2018) 10 NWLR (Pt. 1628) 428 @ Pp. 443-444, paras. H-B.*

The PIA expressly addresses the right of the prospecting licensee to explore the remaining acreage of a prospecting licence, following a conversion of a part to a mining lease.[7] Also, the PIA contains clear provisions on acreages to be relinquished under a PPL, stating that a PPL holder will be required to relinquish:[8]

- parcels of the acreage it indicates to the Nigerian Upstream Petroleum Regulatory Commission (**NUPRC**) that (a) it is not interested in or (b) do not merit appraisal, after declaration of a discovery;
- parcels of the acreage that cover a discovery if after completion of appraisal, it does not declare a commercial or significant discovery;
- parcels of the acreage that cover the retention area if it does not declare a commercial discovery, at the end of the retention period; and
- parcels of the acreage that cover a commercial discovery, if after 2 years of declaring the commercial discovery, it does not submit a field development plan and work.

Conclusion

It goes without saying that if the PIA was the relevant law for the SAPETRO Matter, the outcome would certainly have been different, given that it removes administrative discretion and clarifies the rights and entitlements of the licensee in the various situations. Perhaps the most substantive change is the retention rights, which we believe is a positive signal to investors that their investments in the search for petroleum and addition of new reserves, will not be arbitrarily disenfranchised.

By providing clear guidelines on conversion, establishing retention rights, and enhancing the overall security of tenure for upstream players, the PIA creates a more stable and attractive regulatory framework. As the industry continues to evolve, it is imperative for stakeholders to remain informed and proactive to leverage the innovative provisions of the PIA in navigating their field development efforts.

Disclaimer: This publication is not intended to be comprehensive, nor to provide legal advice. Should you have any questions on issues reported here or other issues in the Nigerian petroleum sector, please reach out to one of the contacts provided below.

Key Contacts:

[7] *Section 81(5) of the PIA*

[8] *Section 78 of the PIA*

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