



CLIENT ALERT

August 15, 2018

3 Things to Note About the New Flare Gas Regulations 2018

The Federal Government of Nigeria (“FGN”) has formally issued the new Flare Gas (Prevention of Waste and Pollution) Regulations, 2018 (“**New Regulations**”), which heralds a new dawn for the gas industry in a bid to make more gas available for domestic use and inch Nigeria closer to ending the harmful practice of gas flaring.

This Client Alert provides an analysis of the following key changes to the gas regulatory regime introduced by the New Regulations:

1. Framework for the National Gas Flare Commercialisation Programme (“**NGFCP**”);
2. Increased rate for Flare Gas payments;
3. Stringent metering and reporting obligations.

1. Framework for the National Gas Flare Commercialisation Programme

The New Regulations essentially lay down the legal framework for the NGFCP of the Ministry of Petroleum Resources. The NGFCP capitalises on the FGN’s right to *take associated gas free of cost at the flare and without payment for royalty*,¹ to grant a new kind of petroleum interest called ‘Permit to Access Flare Gas’ (“**Flare Permits**”) to third party midstream gas project developers (“**Permit Holders**”) via competitive bid processes.² The New Regulations preclude existing Producers from utilising associated gas produced from their fields in such a manner that will affect ‘Flare Gas’³ earmarked for the NGFCP bid processes or concessioned to a Permit Holder. Flare Gas volumes that are not being offered in any NGFCP bid process may however be utilised ‘*for commercialisation*’ by a midstream subsidiary of the relevant Producer⁴ upon application to the Minister of Petroleum Resources (“**Minister**”).⁵

The New Regulations envisage that potential Permit Holders will have to obtain Data Access Permits from the Department of Petroleum Resources (“**DPR**”), which will enable them access data related to the flare sites they are bidding for on a non-exclusive basis. Successful bidders will be granted an exclusive Flare Permit over any flare gas site, to take and utilise Flare Gas from such site on behalf of the FGN.⁶ Consistent

¹ This right currently exists pursuant to Section 9(1) of the Petroleum Act and Paragraph 35(b)(i) of the First Schedule to the Petroleum Act.

² Regulation 2 of the New Regulations.

³ Flare Gas is defined as “*any natural gas produced in association with crude oil by a Producer and finally diverted toward a Flare Site by the Producer with the intent that the natural gas will be flared, including any such natural gas from a Greenfield Project.*”

⁴ This is defined as “*a holder of Oil Mining Lease or an allottee of a Marginal Field*”.

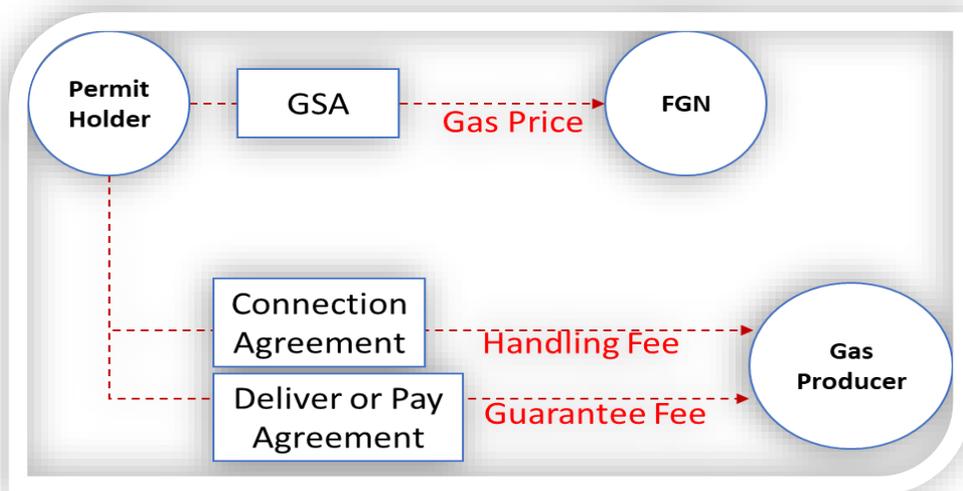
⁵ These subsidiaries may either be existing at the date of the issue of these regulations or planned to be incorporated. See Regulation 3 of the New Regulations.

⁶ Regulations 6-9 of the New Regulations.

with the objective of the FGN’s National Gas Policy⁷ to unbundle the upstream from the midstream gas sector, Producers are precluded from applying for and holding Flare Permits. Specifically, the New Regulations state that Permit Holders must be non-producing companies.⁸

Flare Permits may be revoked in certain circumstances by the Minister; and are transferrable subject to the prior consent of the Director of the DPR. There are fees payable for applications for the Data Access Permits and the Flare Permits, which are to be determined from time to time by the Minister.

The New Regulations contain passive references to the commercial framework for the NGFCP. It envisages that a Permit Holder will enter into a Gas Supply Agreement with the FGN in respect of the sale of Flare Gas by the FGN to the Permit Holder and it also envisages that the Permit Holder and Producer of the relevant flare site will enter into a Connection Agreement to govern the tie-in of the respective facilities of the Producer and the Permit Holder, and a Deliver or Pay Agreement under which the Producer will guarantee to supply Flare Gas to the Permit Holder within an agreed volume and composition range.



To fortify the NGFCP framework, Producers are mandated to provide Permit Holders with access to flare sites and Flare Gas, enter into Connection Agreements with Permit Holders, provide accurate flare gas data, submit required logs and reports, as well as install required metering equipment. Producers who do not comply with these requirements will be required to pay a sum of \$2.50 per 28.317 standard cubic metres (1,000 standard cubic feet or ‘mscf’) of gas flared or vented from the relevant flare site, which shall be in addition to the standard Flare Gas payments discussed below.⁹ Where the Producer continuously breaches the above requirements the Minister may direct the Producer to suspend its operations or outrightly revoke its Oil Mining Lease (“OML”) or Marginal Field award.

⁷ National Gas Policy was issued by the Federal Government on 28th June 2017.

⁸ See Regulation 8(3) of the New Regulations.

⁹ See Regulation 21 of the New Regulations.

Our comments:

The NGFCP is the most innovative gas flare reduction strategy yet and it has the potential to catalyse rapid increase in gas utilisation projects in Nigeria. The New Regulations attempt to provide a clear regulatory framework for the functioning of the NGFCP, which is derived from Section 9(1) of the Petroleum Act and Paragraph 35(b)(i) of the first schedule to the Petroleum Act.

A major concern is that the New Regulations may be challenged by Producers on the basis that it exceeds its legal scope in the following respects:

- excises ‘flare gas’ volumes yet to be produced within an existing OML in favour of third parties;
- prohibits Producers from taking steps to utilize gas even before it becomes ‘flare gas’; and
- mandates Producers to enter into agreements with third parties.

It could also be argued that the New Regulations contradict the basis of the concession granted to Producers pursuant to the Petroleum Act, i.e., to win, work and take away petroleum from the OML area. The key issue therefore is whether the New Regulations can seek to limit the proprietary right granted by the Petroleum Act to Producers, to use gas before it gets to the flare.¹⁰The risk of challenge could perhaps be mitigated if the FGN grants to Producers, a right of first utilisation of associated gas or flare gas at no cost, albeit through a midstream subsidiary. Another mitigation strategy could be to set the proposed Guarantee Fee and Handling Fee to be paid by Permit Holders to Producers at a level that would serve as a commercial incentive to secure the supply commitment of Producers.

With respect to the administration of Flare Permits, the DPR rather than the Minister could have been designated as the authority to grant and revoke the Flare Permits to avoid unnecessary bureaucratic bottleneck in the administration of the NGFCP, especially where, as in the instant administration, the President doubles as the Minister of Petroleum Resources.

2. Increased Rates for Flare Gas Payments

Beyond setting the framework for the implementation of the NGFCP, the New Regulations also complements the Associated Gas Re-Injection Act, 1979 (“**AGRA**”) by clearly setting out the fees to be paid by Producers for routine and non-routine gas flaring as follows:¹¹

- **\$2.00** per 28.317 standard cubic metres (1,000 standard cubic feet or ‘mscf’) of gas for fields producing 10,000 bopd or more per day; and
- **\$0.50** per 28.317 standard cubic metres (1,000 standard cubic feet or ‘mscf’) of gas for fields producing less than 10,000 bopd.

However, where gas is flared as a result of the occurrence of an act of war, community disturbance, insurrection, storm, flood, earthquake or other natural phenomenon that is beyond the reasonable control of the Producer, there will be no liability to make flare payments in respect of the affected Flare

¹⁰ See *MOBIL PRODUCING NIGERIA UNLIMITED V. OKON JOHNSON & ORS (2018) LPELR-44359(SC)*, where the Supreme Court recently held that the process set out in a subsidiary legislation cannot be relied on, where it is at variance with a substantive Act of the National Assembly.

¹¹ See Regulation 13 of the New Regulations.

Gas volumes. There will also be no liability to make Flare Gas payments in respect of any agreed quantity of Flare Gas that a Producer has committed to deliver to a Permit Holder under a Deliver or Pay Agreement as from the commencement of commercial operations of the Permit Holder's flare reduction project, except to the extent that the Producer fails to comply with the New Regulations.

The New Regulations recognise that gas flaring by Producers is subject to the grant of certificates by the Minister as contemplated under the AGRA, and indicates that certificates for continued flaring of gas will be revoked or refused where a Producer fail to comply with the New Regulations.¹² The New Regulations outrightly prohibit Permit Holders and Producers with Greenfield Projects, from flaring or venting gas from their facilities and do not contemplate the payment of flare fees or certificates for them.¹³

Our comments:

The New Regulations provide clarity on the applicable flare payments and quite rightly recognises the need to impose a lower rate for smaller/marginal producing fields. Although an upward review of the flare payments has long been overdue, the increase in fees is considered to be very high – from N10 (approx. \$0.03) to \$0.50/\$2.00. A preferred approach would have been to commence with relatively lower fees that will be escalated annually to discourage prolonged flaring of gas.

The gap of \$1.50 in the flare payments applicable to fields producing less than 10,000 bopd and fields producing 10,000 bopd or greater is significant. Perhaps there could have been a middle-tier band of between 10,000 and 20,000 bopd, where some growing independents and marginal field producers fall.

The New Regulations do not clearly state that Permit Holders are liable to make flare payments for flaring or venting of gas, even though it requires them to report such flaring or venting activity and in cases of routine flaring, prohibits same.¹⁴ The prohibition against routine flaring however appears toothless as there appears to be no consequences for breach. Furthermore, the use of the defined term “routine flaring” in relation to a Permit Holder appears to be misconceived as the term is defined specifically in relation to the operations of Producers and not those of a Permit Holder. A Permit Holder that engages in continuous flaring would therefore not be in breach of the prohibition if the definition of “routine flaring” is strictly applied. These gaps will need to be specifically addressed in the terms and conditions applicable to the Flare Permits.

It would appear that the new flare payments have become applicable as of the date of issue of the New Regulations as the regulations do not provide for a separate date. Thus, the industry will need to brace itself for these new payments even though NGFCP, which is the strategy being adopted to facilitate flare-down, has not been fully implemented. A preferred approach would have been for the New Regulations to state a future effective date for the applicability of the new flare payments to give Producers time to organize their activities.

¹² See Regulations 12 & 14 of the New Regulations.

¹³ See Regulation 12 of the New Regulations.

¹⁴ See Regulations 12, 13, 15(2) & 18(2)(b) of the New Regulations. These requirements may however be imposed in the body of the relevant Permit and made a basis for revocation of the Permit.

3. Stringent Metering and Reporting Obligations

The New Regulations require that measurement of gas flared and vented, associated gas produced and HSE practices relating to these activities must be carried out in accordance with a Metering and Data Collection Standards to be issued within 12 months of the issue of the New Regulations.

The New Regulations place stringent obligations on Producers to provide Flare Gas Data to the DPR within 30 days of such request from DPR. A Producer that fails to honour such request commits an offence and is liable on conviction to a fine of ₦50,000 and/or 6 months imprisonment. This request for data is more circumstantial and is perhaps tied to NGFCP bid rounds.

The New Regulations also require routine logs and reports to be provided by Producers and Flare Permit Holders, i.e.,:

- daily logs for gas flared and vented to be submitted to the DPR within 21 days of the end of the relevant month;
- daily records of associated natural gas produced to be provided to the DPR within 21 days of the end of the relevant month; and
- annual reporting of previous year Flare Gas Data submitted by 31 March of each year to the DPR.

Failure to provide these logs and reports to the DPR within the prescribed timelines will make Producers liable to pay a \$2.50 fee per 28.317 standard cubic metres (1,000 standard cubic feet or ‘mscf’) of gas flared or vented from the relevant flare site or result in the revocation of OML/Marginal Field awards as indicated earlier in this note and Permit Holders may lose their permits.

The DPR is also required to release an Annual Report containing useful information on associated gas production and flaring for the previous year by 30 June of each year.

Our comments:

The introduction of these metering and reporting obligations are welcome and will be critical to the successful implementation of the NGFCP and the regulation of the gas industry going forward.

As the EGASPIN already contains elaborate provisions on metering, HSE and reporting obligations in relation to gas flares and gas production generally, perhaps efficiencies could be gained by recognizing the relevant provisions of EGASPIN as the applicable standards, as opposed to developing an entirely new set of rules.¹⁵

¹⁵ The EGASPIN (Part III & V) provide for self-reporting of gas flares and metering standards.

While this Client Alert is not intended as legal advice, we hope you have found our review of the New Regulations and comments useful and are available to provide advice on any of the issues raised as well as its possible impact on oil and gas operations in more detail.

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