PRODUCTION SHARING CONTRACT IN THE NIGERIAN OIL AND GAS SECTOR

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Nigeria had in the past years engaged in Joint Venture Agreement (JVA) for the exploration of her petroleum resources. This JVA in Nigeria was associated with poor funding, due to the imbalance in the financial capacity of the different Joint Venture Partners, especially the Nigerian government which has other pressures on its resources. This led to the reduction in oil operation and consequential loss of revenue.

Consequently, the expansion of the Nigerian oil and gas industry led to the allocation of acreages in the shallow and deep offshore areas to foreign oil companies. This increased the need for a different policy in the oil and gas sector, as the expansion brought its own challenges in terms of funding and technical complexity.

In the bid to overcome these challenges, enhance the country's oil reserve and improve the economy of the country, Production Sharing Contract (PSC) was introduced as a policy for the exploration of the country's petroleum resources.

This policy is mainly regulated by the Deep Offshore and Inland Basin Production Sharing Contract Act, Laws of the Federation of Nigeria 2004 (volume 5).

Under this policy the Nigeria National Petroleum Corporation (NNPC) a governmental agency engages a competent contractor (Petroleum Exploration and Production Companies or its Subsidiary duly registered in Nigeria) to carry out petroleum operations in Nigeria.

The contractor undertakes the initial exploration risks and if oil is discovered and extracted, the contractor will be allocated a portion of the oil produced sufficient to reimburse its costs of production (cost oil), as well as payment of royalty (royalty oil) which is fixed in accordance with the location of the oil field such that the deeper the concession is from onshore, the lower the royalty rate that is applicable. Also from the production, a portion will be allocated as tax to the Nigerian Government (tax oil). What ever remains after these deductions shall be shared among the parties by the ratio stated in their agreement (profit oil).

In the PSC policy the concession ownership remains entirely in the NNPC. However, on production its interest and title are attached to usually a higher percentage of the profit oil. The contractor is permitted to market the portion of the production allocated to

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cost oil, tax oil, and contractor's share of the profit oil but at the price fixed by the NNPC. No doubt this puts Nigeria in charge of her oil and gas sector.

Certainly, the contractor bears all initial costs of the oil operation, though gets reimbursed through the allocation of Cost Oil. Nevertheless, the reimbursement of such cost only occurs on the discovery and production of commercial oil reserve. No contribution from the NNPC when there is no production.

It is apparent that the policy is rewarding to both Nigeria and the contractors, it is also preferable as it is relatively flexible in the management of the country's oil production, and the fact that it lifted the financial burden from the host country. Nigeria now focuses on other areas of her economy while trusting that the oil and gas industry will be developed without the usual trappings of cash call constraints.

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