TEMPLARS

UPDATE: NEW GUIDELINES ON THE MINISTER'S CONSENT TO ASSIGNMENT OF INTERESTS IN OIL AND GAS ASSETS

Recently, the Department of Petroleum Resources (*regulator of Nigeria's petroleum industry*) issued the "***Guidelines and Procedures for Obtaining the Minister's Consent to the Assignment of Interest in Oil and Gas Assets, 2021***" (the "**New Guidelines**"). The New Guidelines repealed and replaced the Guidelines and Procedures for obtaining the Minister's Consent issued in 2014 (the "**Repealed Guidelines**").

Our Newsletter highlights the significant changes and the practical implication on assignment of oil and gas assets.

What Constitutes an Assignment?

Assignment is defined in the New Guidelines as the transfer of:

- an oil prospecting licence ("**OPL**"), an oil mining lease ("**OML**"), marginal field ("**MF**"), an oil or gas pipeline ("**OGPL**"); or
- an interest, power or right in an ***OML***, ***OPL***, ***MF*** or ***OGPL***.

Who can Assign?

Any company or person with equity, participating, contractual or working interest ("***Interest***") in the ***OPL***, ***OML***, ***MF*** or ***OGPL*** (***"Licence or Lease"***) may assign such Interest.

What Constitutes an Interest in a Licence or Lease?

It is instructive to note, per the Guidelines, each of the following may qualify as an "Interest" in a Licence or Lease:

- Interest of a Production Sharing Contractor in a Production Sharing Contract.
- Interest of a Party in a Production Sharing Agreement.
- Interest of a Concessionaire as a Participant in an OML, OPL, MF, or OGPL.
- Interest of a Farmee or Farmor in a Marginal Field.
- Interest of a Sole Risk Concessionaire in an OML, OPL, or MF.
- Interest of a Service Contractor in a Risk Service Contractor or perhaps, a Strategic Alliance Agreement.

In addition to the foregoing and similar to the provisions of the Repealed Guidelines, there is an ambiguous category which deems any other business arrangement (*by which a right, privilege, power, benefit, gain or advantage in a Licence or Lease is transferred to or conferred either directly or indirectly on a third party*) as an Interest in a Licence or lease.

Importantly, charges and liens are now included in the definition of Interest which will have a significant impact on existing and future financing of upstream assets..

Ambiguities

Again, the Department of Petroleum Resources ("**DPR**") missed the opportunity to clarify the uncertainties that have bedeviled the interpretation of *other business arrangements that confer a right, privilege, power, benefit, gain or advantage in a Licence or Lease*. **What does this mean exactly?** Would it include the interest of a funding and technical services provider under a Funding and Technical Services Agreement purely because the services provider is entitled to a benefit, an exclusive funding privilege or a first ranking right to the cash-flow? Would it include the interest of a strategic alliance partner under a strategic alliance agreement? The questions are endless.

Another complication is the inclusion of *charges and liens* in the definition of Interest as the creation of security (including floating charges) over an OPL, OML, MF and OGPL may now require the consent of the Minister at the point of creating the charge as opposed to market practice of deferring the procurement of consent to the point of enforcement of the security interest.

These issues above are expected to heighten completion risks in upstream oil and gas financings and increase financing and transaction costs.

Forms of Assignment

Similar to the Repealed Guidelines, the New Guidelines provide a list which is by no means exhaustive but gives an indication of the forms of assignment. These include assignment by way of exchange or transfer of shares; private placement or public listing, merger, acquisition, business combination, acquisition, take over, divestment, internal re-organisation, devolution of shares by operation of law or testamentary device.

Ambiguities

The New Guidelines state that the appointment of a receiver, receiver/manager or administrator under the Companies and Allied Matters Act or any other comparable legislation in a foreign jurisdiction constitutes a form of assignment. This introduces another complexity as t the consent of the Minister will be required to effect the appointment of a receiver, receiver/manager or administrator (such being an assignment) and perhaps, validate the steps taken by such officers afterwards. If required, this will result in an elongated timeline for completing the engagement of these officers. It is also not clear what the reference to any other comparable foreign legislation denotes.

In relation to the assignment of Interest by a parent, and akin to the Repealed Guidelines, the New Guidelines do not assume that every transfer of shares or Interests by the parent or affiliate of a participating interest holder constitutes an assignment. The DPR is obligated to lift the veil and come to a determination on the nature of the transaction and whether it constitutes an assignment. However, the New Guidelines provide no guidance on how the the veil lifting exercise will be initiated. Should the parent or affiliate self-report or seek a negative clearance to avoid such intrusive veil lifting after the consummation of the transaction? There are no objective indices for coming to such determination. Where does the DPR draw the line – at the "***parent- subsidiary level***" or at the "***intermediate company level***" or will this go as far as clawing at a transfer of shares that occurs at the ultimate beneficiary's level? These are grey areas the market would have expected the New Guidelines to resolve.

Reassignment

Reassignment is an entirely new construct introduced by the New Guidelines It is defined as a situation where there has been consent to an assignment of Interest and the parties subsequently, whether by mutual consent or by operation of law, sever their relationship and the assignor wishes to obtain the consent of the Minister to revert the interest. A reassignment, under these circumstances, can only be made to the original assignor and not a third party. The instances that readily come to mind are instances where the Minister has consented to the creation of a mortgage, charge or lien over an OPL, OML, MF or OGPL and the security provider (i.e. the assignor of the security interest) following full and final repayment of the underlying debt, seeks the release of the security interest created. It is not clear if a Reassignment will attract the consent fee and the New Guidelines do not outline the process for seeking the consent of the Minister for a Reassignment. If the Interest is being reassigned to the original assignor, the process should be less rigorous than that stipulated for an assignment and the consent fee should also be negligible.

Protecting New Entrants

The New Guidelines introduce some concepts which are aimed at protecting the interest of new entrants and the NNPC specifically in assignment involving a direct transfer of the licence or the lease.

Crude Handling / Crude Purchase Agreements

In a bid to protect new entrants from inheriting legacy contracts and assuming legacy liabilities, the New Guidelines prohibit an assignor from imposing a crude handling or crude purchase agreement on the prospective assignee as a condition for the consummation of an assignment amongst other conditions that may impede the takeover and / or operation of the asset in a business-like manner.

The New Guidelines also require that where the assignment is by way of a direct transfer of the participating interest held in a joint venture with the Nigerian National Petroleum Corporation (**NNPC**) and such transaction involves the execution of a crude handling or crude purchase agreement, the assignor must submit a copy of the draft agreement to the DPR before execution. This adds to the documents required to be submitted in connection with divestments by IOCS... It also subjects the agreements to the scrutiny of the regulator and may thus strengthen the prospective assignee's bargaining power and ability to push back on unfairly balanced provisions in the legacy agreements. Typically, direct asset transfer by IOCs would involve the execution of crude handling and offtake agreements.

Asset Valuation

The New Guidelines provide certain directions in the valuation of an asset by the assignor and assignee. For instance, where the investment on surface facilities has been fully amortised through cost recovery, the assignor shall not include such facilities as part of its valuation of the asset. This is aimed at ensuring that assignors who have recouped their capital investment through the cost recovery provisions of their relevant operating contracts do not earn additional revenues on the relevant capital assets from the assignment transaction.

Further and similar to the Repealed Guidelines, the DPR is required as part of its due diligence, to consider the pricing of the asset to ensure that there is no adverse effect on the revenue of the Federation and the reference value of an asset shall be the book value. Put differently, where the asset valuation for the assignment transaction does not reflect the book value, the DPR may refer to the book value in the determination of the consent fee (5% - 10% of the transaction purse) to ensure that the Government's revenue from the assignment transaction is not eroded through the creativity of the transacting parties.

Abandonment and Decommissioning Liabilities

To ensure that abandonment and decommissioning liabilities (albeit contingent at the time of the transaction) are not fully dumped on the new entrant and the NNPC, the assignor has a mandatory obligation pursuant to the New Guidelines to submit to the DPR an agreement between the transacting parties on the treatment of the assignor's abandonment and decommissioning liabilities. The agreement is expected to quantify the cost of the abandonment and decommissioning liabilities and such cost is expected to be deducted from the transaction purse. *This is an unprecedented development and clarity is required on the following: the methodology for computing the cost of the liabilities, the tax treatment of the cost deducted from the transaction purse, the provisioning and the custodial arrangement for the abandonment and decommissioning funds, etc.*

Precursor to the Minister's Consent

Notification of Intention to Assign

The New Guidelines have clearly defined a two-tiered notification process that must be adhered to by the prospective assignors prior to the application for the Minister's consent.

The first step requires the assignor to notify the DPR in writing of its intention to carry out an assignment. Although, the DPR does not provide any guidance on what constitutes an "assignor's intention", it is not unreasonable to argue that this obligation will be triggered once the assignor comes to a decision through a board resolution, shareholder resolution or management decision. In a bid to facilitate ease of business, the New Guidelines impose an obligation on the DPR to respond to the notification within ten (10) working days from the date of receipt of the notification, failing which the assignor may proceed to the next stage of the assignment process on the basis of a deemed approval.

Notification of Prospective Assignee

Upon the completion by the assignor of the technical evaluation of companies shortlisted for the Assignment (and akin to the Repealed Guidelines), the assignor is required to submit the shortlist to the DPR. The prospective assignor will not be eligible to submit an application for the Minister's consent if it fails to fulfil this obligation. The DPR is required to respond to the notification within ten (10) working days following the receipt of the notification. However, the DPR's approval will not be deemed in the absence of a response. The New Guidelines do not provide any guidance on the practical remedy for an assignor if the DPR disregards the timeline. This may be a deliberate omission given that this is the stage at which the DPR evaluates the acceptability of the shortlisted assignee to the Government. Therefore, it may be risky for a prospective assignor to proceed to the commercial stage without the required clearance. Although, it could be argued that reliance may be placed on the Executive Order on the Promotion of Transparency and Efficiency in the Business Environment (the **"Executive Order"**) which introduced the concept of deemed approvals into our legal space, the recent attitude of Nigerian courts indicate that such reliance may not be fool proof.

Similar to the Repealed Guidelines, the New Guidelines stipulate that it is the responsibility of the assignor to secure the consent of the Minister. However, the New Guidelines disapply this rule in the case of assignment by operation of law. This clarification is necessary given that the assignor will be the adversely affected party in an assignment triggered by operation of law and will not, as a practical matter, be expected to take any step inimical to its interest, such as seeking the consent of the Minister.

Separation of the Subsurface Assets from the Associated Pipelines

In relation to assignments of interest in assets jointly owned by the assignor and the NNPC, particularly where the assignment involves the transfer of subsurface rights, and interests in associated pipelines, the New Guidelines require the application for the Minister's consent to the transfer of interest in associated pipelines to be separate from the application for the Minister's consent to the transfer of the subsurface rights.

The implication is that two separate applications would be required, the consideration for the grant of consent may also differ resulting in a situation where the prospective assignee may be granted consent for the subsurface rights but denied consent in relation to critical infrastructure (i.e. associated pipelines). The obligation to submit separate consent applications may also encourage transacting parties to enter into two separate assignment agreements. However, if the advisory team is not careful and deliberate in the drafting and the definition of the consideration in both assignment agreements, there may be double counting of the aggregate consent fees thus increasing the cost of the transaction.

Due Diligence

Similar to the Repealed Guidelines, the DPR is obligated to conduct due diligence on the assignee. While under the Repealed Guidelines, the purpose of the due diligence was to establish the technical competence and financial capability of the assignee, the New Guidelines extend the objectives of the due diligence exercise to include the determination of the legal status of the assignee, the history of the assignor's relationships with previous assignees, the history of compliance with the provisions of the Petroleum Act or Oil Pipelines Act and the assignor's track record on the operation of the asset. Further, in line with the general theme of the New Guidelines for the provision of timelines for the different activities of the DPR, the due diligence exercise must be conducted within sixty (60) calendar days from the date of receipt of the complete application.

Interestingly however, the New Guidelines do not impose a timeline for the grant / refusal of the consent of the Minister. Industry players will now turn their attention to the outcome of the discussions and debates on the Petroleum Industry Bill currently at the National Assembly, the current draft of which contains a timeline as well as a deemed approval where no feedback is provided within the timeline.

Applicable Fees

Given the changes in applicable fees as provided under the Petroleum (Drilling and Production) (Amendment) Regulations 2019 (**"PDPR"**), expectedly, the application fee and premium payable on assignment transactions have been updated with relevant references made to the PDPR. The applicable fees are now as follows:

- Application fee for assignment of OML: US$10,000.
- Application fee for assignment of OPL: US$5,000.
- Application fee for assignment of a marginal field: US$2,500.
- Premium: 5% to 10% of the total value of the transaction.

However, given that the PDPR is made pursuant to the Petroleum Act and does not provide for the fees payable for the assignment of interest in an oil or gas pipeline, the applicable fee payable for the assignment of interest in an oil or gas pipeline is unclear.

First Consideration for Nigerian Companies

Unlike the Repealed Guidelines, there is no requirement in the New Guidelines for a prospective assignor to give first consideration to Nigerian indigenous companies in assignment transactions. However, the omission does not relieve a prospective assignor of this obligation as a similar provision is already contained in the Nigerian Oil and Gas Industry Content Development Act, 2010.

Register of Assignments

The DPR is required to maintain a register of assignments to which the Minister has consented. This mirrors a similar provision in the Petroleum industry Bill currently before the National Assembly. This should assist the regulator, advisors and relevant stakeholders in tracking changes in the incidences of ownership of OML, OPLs, MFs and OGPLs

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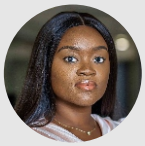

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