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## Article

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## Annulment of Oil Licences in Nigeria's Upstream Petroleum Sector: A Legal Critique of the Costs and Benefits

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### ABSTRACT

Owing to various reasons, tenable and untenable, successive governments in Nigeria have annulled licenses duly granted to identifiable upstream petroleum operators. With due sense of circumspect, when irregularities manifest in the process and the grant of substantive licences, such does not vest in the government an unfettered right to annul the licence. There are evidences of such occurrence in spite of established procedures regulating annulments, commonly referred to as revocation or cancellation. This paper is a critique of the annulment of oil licenses and the associated contractual-regulatory dimensions. The validity of the Federal Government's actions also comes to the fore, particularly in the light of renewed drive to attract investments into the upstream sector. Thus, as some benefits are accruable to the players, it is also important to appraise the consequential costs attributable to undue annulment of oil licenses. The paper adopts a descriptive analytical method of available facts, expounds requisite statutory provisions and utilizes judicial precedents to highlight the context of the study. It is imperative that the Federal Government adheres to established procedures on oil license annulment, as a contrary posture will amount to several negative outcomes.

**Keywords:** Oil, Upstream, Nigeria, Licence, Annulment, Contracts, Regulations

**JEL Classifications:** K32, K12, K2, K42, P28

### 1. INTRODUCTION

The recent decline of global oil prices (2015-2017) has not diminished the significance of oil and gas revenues to Nigeria's socio-economic and political well-being. Earnings from oil, gas and associated products remain the mainstay of Nigeria's economy but there are current efforts to diversify the national revenue base. This progression can only be effectively achieved by leveraging the sanctity of established processes and practices that are integral for the sustainability of Nigeria's oil and gas industry.

The seemingly customary practice of revoking, cancelling or annulling various species of oil agreements is no longer tenable and is evidently inconsistent with industry best practices. It apparent that such a posture clearly contradicts the desire and efforts to secure long-term financing of upstream projects. The reasons for adopting annulment is usually hinged on intrinsic right, albeit unilaterally, to review and reevaluate subsisting agreements, notwithstanding the pending contractual obligations (Akinrele, 2016). The considerable losses, financial and otherwise associated

with breaches in procedure needs to be urgently addressed, if all the stakeholders (internal and external) are to derive optimal benefits. Moreover, the multifaceted collateral damage associated with oil and gas activities is well documented (Oyewunmi and Oyewunmi, 2016) but the Nigerian State can ill-afford to perpetuate a negative perception on issues of due commercial compliance. Evidently, such unfavourable outlook, coupled with other impediments, has hampered sustained investments into the upstream petroleum sector. A concerted and holistic policy driven approach will contribute in measurable respects to mitigating negative outcomes in this regard.

The upstream license award process is complex, competitive, capital intensive, potentially profitable and involves multiple interests (Atsegbua, 2004). In Nigeria, the right to participate in the upstream sector is usually granted on the basis of licences or leases. This will typically refer to the; oil exploration license (OEL), oil prospecting licence (OPL) and oil mining lease (OML); all of which vary in terms of tenure, geological coverage and permissible activity (Nlerum, 2007-2010). Hence, owing to the

multiple layers of risk associated upstream sector, the principal actors need to fulfill their reciprocal obligations, failing which will culminate in added costs and consequential losses for both parties.

Annulment of oil licences is comparable to the proverbial double 'edged sword' with divergent outcomes, subject to the decisions made by the contracting parties relative to a given set of circumstances. On the one hand, the enabled statutory governmental agency must ensure that annulments are effected based on the express provisions of applicable laws. Thus, it will not suffice to annul oil licences merely on policy inclinations or other extraneous matters not under consideration during the award process. Whilst on the other hand, the licensee may bear the burden (annulment) of not adequately fulfilling the terms and conditions underpinning the grant of a licence. This is in spite of the fact that considerable levels of investment have been committed towards commercializing the grant coverage area.

The principle of privity to all intents and purpose provides a veritable benchmark for effective regulation of contractual interactions. The primary statute, requisite award rules and guidelines; and the express, implied and customary licence terms, are integral to determining the validity of annulment. In the light of varying contractual complexities, this paper entails a legal critique of costs and benefits connected with the irregular or arbitrary annulment of oil licences in Nigeria. The paper addresses a sensitive and somewhat controversial subject matter, especially in the light of the myriad of interests competing for a share of the common wealth of the Nigerian State. In the process of securing specific allocations, there are bound to be some breaches or omissions by the certain players or stakeholders. The following paragraphs, constitute conceptual clarifications, legal framework for investment guarantees, statutory overview, judicial critique and conclusion.

## 2. CONCEPTUAL CLARIFICATIONS: AWARD OF LICENCES AND ANNULMENTS

An OEL encapsulates the express consent granted by a competent authority to execute specific undertakings within a delineated geographical area. Hence, failure or omission to secure the requisite consent renders subsequent actions by an affected party illegal or wrongful. In a more concise sense, it entails an authority to do something, subject to the stipulated terms and conditions. A licence as opposed to ownership vests limited or qualified legal interest, coupled with the fact that it is also revocable subject to a contract duly signed, sealed and delivered by the respective parties. Licensing in the upstream petroleum sector refers to authorization given by the Federal government to upstream petroleum companies to carry out certain activities as expressed and implied by the licence. According to section 2(1) (c) Petroleum Act 2004, licenses in the oil sector are commonly referred to as concessions or leases and are usually granted in wide and extensive terms, that is, "to explore, acquire, produce and to dispose of petroleum."

Hence, it is erroneous to construe, that the Federal government as the original titleholder, has transferred the unqualified degree of title to a licensed operator. Moreover, the applicable laws of

Nigeria do not recognize the private ownership of oil and other mineral resources, which further attests to the limitation on oil exploration rights or interests and by implication affirming the dominant role of government in the scheme of oil development affairs. The Minister of Petroleum usually awards OEL in accordance to section 2(1) of the Petroleum Act, Laws of the Federation of Nigeria. It empowers the licensee to venture into petroleum activities in the area encompassed by the licence. In addition, the licensee is statutorily enabled to commence exploration activities not later than 3 months after issuance of the licence. By virtue of the provisions of the Act, OEL expires on December 31<sup>st</sup> of the year following the date of issue, but it may be recommenced for another year.

As regards the OPL, the Minister for Petroleum may grant such pursuant to section 2(1) (b) of the Act. It offers the holder of the licence the power to delve into activities oil within the area covered by the license. The Petroleum Minister in accordance with section 2(1) (c) petroleum act awards an oil-mining lease (OML). An OML is exclusive to the holder of an OPL who has met all the provisions stipulated on his license; has found oil in market able magnitudes and achieved minimum oil production benchmark of, 10,000 barrels of oil per day relative to the licensed area for prospecting. Under paragraphs 8, 9, 10, 11, 12 and 13 of the 1<sup>st</sup> schedule, petroleum act, the holder of Oil Mining Lease enjoys all the rights of an OPL holder. This is inclusive of; exclusive rights to explore, acquire, operate, and remove and to sell the crude oil found and explore in the area subject to the terms of the lease or the concession. The act, also the vests in the Minister of Petroleum; powers over the allotment of licenses for prospecting, mining exploration of oil without deploying the requisite oversight controls for regulating the process of such allotments. It is noteworthy that under Nigeria's constitution and established administrative law principles clearly indicate that; where the law stipulates a specific process for exerting a right, the processes must be stringently complied with in the exercise of such power. Thus, adopting an alternative approach is illegal especially if the law relates to repudiation of the proprietary right of citizens.

Successive administrations, have allocated oil licenses covering exploitation of oil resources, without instituting effective procedures that regulate such a complex and multifaceted process. Such a posture has evidently provided ample opportunity for entrenching unethical and corrupt practices on the part of some operators, as well as notable regulatory authorities. During the military rule, most licenses were awarded without due process by the Heads of State. In 1999, the former President Chief Olusegun Obasanjo annulled eleven oil blocks awarded to the former military officers by the previous governments. 67 licenses were granted between January 1, 2005-December 31, 2011 with \$506 Million outstanding unpaid signature bonuses to the Federal government account. 7 discretionary allocations reviewed, \$183 Million was alleged outstanding and due to the national treasury (Ribadu, 2016).

The likelihood of abuse is predominant during award of oil licenses, and more so as the process is often based on direct negotiations with prospective operators. Auctions procedures are imperative in the selection of the most competent operators for production.

Pre-qualification process ensures that companies that participate in tender process are competent to execute the contract. Fraud may also arise where criteria for pre-qualification is structured to single out certain operators. Instructively, the adoption of 'right of first refusal' option accorded to specific participants in the bidding process may breed corruption and other rent-seeking activities that are detrimental to the myriad of stakeholders. Government officials and regulatory authorities can exploit such gaps to extract bribes from the bidding companies. Also captured is infringement of due process by disclosing sensitive facts to one of the bidders in advance in exchange for favour and other rent seeking behaviour. Furthermore, abuse occurs; when the licensee violates the terms of the licence, under quoting volumes and government officials are culpable of not delivering monitoring and oversight functions, as they ought to. Consequently, renegotiations and amendments are inevitable in a contractual regime bedevilled with compliance practices or incidents. It also negatively affects the expected revenues attributable to anticipated production activities over a given period.

### 3. INVESTMENT GUARANTEES IN NIGERIA: OVERVIEW OF LEGAL FRAMEWORK

Successive Nigerian governments have often expressed the desire to attract foreign investment to the upstream sector. The efforts in this regard have without a doubt yielded a notable number of laws, even though the level of harmonization is subject to ongoing debate. A non-exhaustive list of such laws includes; Investment and Securities Act, 2004; Nigerian Investment Promotion Commission Decree; National Office for Technology Acquisition and Promotion Act, 2004; Companies and Allied Matters Act, 2004; The Nigerian Content Development Act, 2010, Foreign Exchange Monitoring Miscellaneous Provisions Act C 2004, Industrial Inspectorate Act Cap.18, Laws of Federation of Nigeria, 2004, and 1995, the Privatisation Decree, 1999.

It is a fact that such legal frameworks irrespective of the good intentions underpinning such, have not sufficed to mitigate the investments risks in Nigeria. What is more fundamental towards sustaining the required investments is the recurring issue of consistent levels of implementation. In addition, the issue of policy review needs to be frontally addressed, subject to unfolding realities. Hence, such a posture will contribute towards; creation of viable investments opportunities and climate; ensure fairness and equity; promote rule of law and probity, and ultimately entrench a culture of due process in the award of licences for upstream players. The Petroleum Act failed to explain the specific attributes of an oil license, especially in terms of whether it vests exclusive rights on the holder. It gives extensive right to the lessee to search for oil, to utilize oil-mining lease, and to refine the oil. The "without restrictedness" connotes that on no account will any other stakeholder be awarded a privilege to search for crude on the field covered by the earliest license granted until after it expiry. In effect, such a license may be annulled if it is transferred for value without the consent of the Minister of Petroleum and Energy Resources.

Alternatively, oil-prospecting license offers the licensee specific privileges. It gives the right, the privilege to search, dig for oil

within the scope of the licence. Lessee may transfer the license with the consent of the Minister of Petroleum and Energy Resources with the right to dispose of oil won during the prospecting activities in the sector. These privileges are exclusive it offers rights that are profitable and commercially significant to the licensee. The Minister cannot suo motu terminate the contractual oil licence without following due process. Any indiscriminate annulment amounts to a breach of contract and by implication contravenes section 44 of the 1999 constitution of Nigeria that guarantees inviolability of right to property anywhere in Nigeria. Furthermore, any alteration of the sum of royalty payable by the licensee; or any other terms not in the licence that was introduced subsequently after the agreement has been executed and prescribed statutory fees have been paid; or any other reasonable commercial considerations that were not anticipated by the parties, is an expropriation of the licensee's exclusive possessory right. An annulment of the oil license, while there is a subsisting oil licence contract makes the Federal Government liable for breach of contract and infringement of the licence's right to property.

### 4. ANNULMENT OF OIL LICENCES: A STATUTORY OVERVIEW

The unilateral revocation of oil licenses on the part of the Federal Government, before the expiration period and without any merit, is to all intents and purposes a breach of contract. It further entails, a confiscation of value, depriving the licensed operators their rights and benefits accruable to them in the course of their undertaking. The government's action in this regard has increased licensees' investment risk exposure in the sector. This is coupled with the fact that such infringes the statutory guaranteed and exclusive rights allocated to licensees under the requisite laws and regulations governing such matters. The Federal Government will usually be inclined to annul subsisting oil licences as part of ongoing efforts to combat corruption in the oil and gas sector. It centres on expediency for the adoption of such an option, especially where beneficiary companies have failed or neglected to pay statutory application fees. Moreover, as formal agreements governing the entire undertaken are still being finalized, a window of opportunity may exist to annul contractual obligations.

By virtue of the provision of paragraph 23(1) of the first schedule to the Petroleum Act, the Minister of petroleum may annul any oil licence if the licensee is being managed by a citizen or a company registered in any country other than Nigeria and where the laws do not permit Nigerians to run petroleum concessions on certain conditions which in the opinion of the Minister of Petroleum and Energy Resources is similar with the terms upon which such concessions are given to citizens of such foreign investor in Nigeria. Also, in paragraph 24 of the same First Schedule to the Petroleum Act further provides that the Minister of Petroleum and Energy Resources can annul OPL or oil mining lease to OML, if in his estimation, the concerned licensee or lessee is not carrying on its operations regularly and in a business-like tactics worthy of oil field practice, or refused to adhere to the provisions of the Act or any other procedures or failed to honour his duties as stated in the license or lease or failure to pay outstanding royalties, if



demand for or not by the Minister within the time stated or in accordance with Act or has refused to make available such details on his activities as the Head of Petroleum Inspectorate demand. The licensee or lessee shall become liable for all liabilities suffered before the actual date of such cancellation.

According to Etikerentse (2004) on the effectiveness of the power of revocation of petroleum licence, he said that:

*"The significance attached to the cancellation powers of the grantor in this issue has been taken away to a great extent by the very fact that in nearly all petroleum operations in Nigeria now, the Government through Nigerian National Petroleum Corporation has participation interests. Nigerian National Petroleum Corporation's officials have a say in the manner the processes are carried out and they would therefore be aware of any non-payments that warrant of annulment. Annulment would thus affect both parties to the joint venture and the Nigerian National Petroleum Corporation's inspectorate, being the actual organ saddled with effecting any annulment, would be most unwilling to carry out that order that would indirectly affect its alter ego."*

Evidences abound of instances when the Federal Government had cancelled licences awarded by the previous governments. Notably, in 2011, Eni and Shell petroleum Companies were alleged to have paid \$1.1 Billion for oil block OPL 245. The payment was allegedly made to the Federal government, who then passed it on to Malabu Company owned a former Nigerian oil minister who during his tenure in office, had awarded the oil block to his own company. The Halliburton case is also worthy of mention as the company officials conceded that its Nigerian subsidiaries sometime in 2006; offered bribes of \$2.4 million dollars to tax officials for favourable tax rebate worth more than \$14 million. The company's licence was consequently annulled as the matter is currently pending at the Federal High Court. The unilateral annulment has also brought to the fore legal and policy inconsistencies touching on the validity of annulment process, as well as the associated contractual consequences. It thus suffices to say that the implementation of the extant legal framework is weak, as there is need for concerted effort to achieve the desired outcomes in upstream sector.

## 5. JUDICIAL CRITIQUE: OIL LICENCE ANNULMENT IN NIGERIA

In the decided case of; Mr. Obikoya and Sons Nigeria Limited V. The Lagos State Governor, the court stated that any law that governs mandatory acquisition of the citizen property right; such must be interpreted firmly against the acquiring party to the benefits of the title holders of the acreage or the party in possession of the property in question. The Petroleum Act, the principal legislation regulating oil search and production, stipulates the procedure by which the Minister for Petroleum can revoke oil license where foreigner is controlling the license. Paragraph 23(1) (a) of Schedule 1 to the Petroleum Act amongst others provides for revocation; where in the Minister's opinion,

the lessee or other stakeholders fail to honour the Act or fail to fulfill his expected duties in paragraph 24 (1) and lastly to pay royalties even if not demanded by the Minister. However, the Minister can only exercise such power after satisfying the prerequisites stated under paragraphs 25-29 of the Schedule. Paragraph 25 inter alia states that the Minister must notify the licensee the grounds for the revocation. Licensees are to be giving the reasons and where the Minister is contented with the reasons, he may summon the licensee to make amendment in respect of licence or other issues within the shortest time as enshrined in paragraph 26 of the Act. Where the leaseholders fail to give cogent reasons, or amend the complaint within the time framed, the Minister may then annul the license as stated under paragraph 27 of the Petroleum Act.

The revocation exercise by the Federal government contravened the "due process" and doctrine of "natural justice." Section 36(5) and section 44(1) 1999 of the Constitution (as amended); provides for fair hearing on matters of individuals' civil rights and civil obligations. It also nullifies compulsory acquisition of private property except in accordance with the law. Failure of the Federal government to conform to the statutory procedure for revocation of oil licences renders such revocation null and void. It is trite law that, before licensees' proprietary rights can be varied or revoked such licensees must be accorded the full privileges of fair hearing.

In Lagos State Development and Property Corporation V. Foreign Finance Corporation, it was opined that a holder of administrative authority must give the person who is going to suffer injury by the use of such administrative authority reasonable trial. It is a mandatory prescribed procedure and non-compliance renders the action or process a nullity. The Supreme Court declared that in the exercise of revocation power, the potential party must be given an opportunity to be heard, as the exercise may touch on their exclusive right. For instance, when government official is exercising the powers conferred under Section 28 of the Land Use Act 1978 to annul the Certificate of Occupancy issued through the power of cancellation he or she is expected to act with reasonable fair hearing and to respect fundamental human rights of the parties to such contract.

Also, in Ude V. Nwara, the court held that where the law gives powers with the effect of extinguishing exclusive rights it is expected of those exercising such powers to strictly adhere to the provisions of the law. Anybody who performs public duty are expected to comply with the rule of law; to exercise their discretion judiciously and in conformity with the enabling statute. Upstream petroleum companies who held the licenses that had been annulled by the Federal government alleged denial of fair hearing. The Committee of Inquiry established by the Federal government to consider the procedure for the award of the grant and it was on the findings of the Committee of Inquiry that the Federal Government cancelled the licenses of concerned Companies without prior notices. Furthermore, even when the concerned upstream companies failed to pay up the outstanding prescribed statutory fees; that do not give the right to annul the licenses contrary to the provision of the

enabling law. An infringement of any covenant in oil licence agreement only establishes basis for annulment but may not definitely result to annulment. As decided in *Nwara (supra)*, an infringement of terms in an oil licence agreement is a mere ground for forfeiture. It is thus evident that the annulment by the Federal government was not consistent with the Petroleum Act and the 1999 Constitution of Nigeria (as amended). Therefore, the annulment was illegal, null and void. In a more recent case, Federal Government revoked, the OPL 323 that had been allotted to the Korea National Oil Corporation in August 2005. Nigerian government alleged that the Korean National Oil Company is yet to pay the balance of \$231 Million signature bonus on the two oil blocks allocated to it. The revocation was executed while the court had granted an order of interim injunction against the Attorney General of the Federation and the President, Federal Republic of Nigeria restraining them from the revocation of OPL pending the determination of the substantive matter before the court. The Federal Government instituted an action at the Federal High Court, Abuja with an application for a stay of execution stating the reasons it has not obeyed subsisting court orders that rendered void the annulment of OPLs 321, 323 respectively. The court decided that the annulment of the two OEL of the foreign conglomerate Company by the Federal government was illegal, particularly on the grounds that Federal Government did not have the legal powers to revoke OEL. Hence, it suffices to say that the Minister of Petroleum and Energy Resources is the appropriate authority in this regard.

The legal interpretation of schedule 4 of the Petroleum Act is fundamental to the holistic appreciation of the legal essence as well as the associated consequences oil licence annulments. It provides, that any licence or lease granted under an enactment repealed by the Petroleum Act shall continue in force notwithstanding the repeal, but shall be subject to the Petroleum Act and to any regulations made thereunder except on matter of; duration of the licence or lease, rent and royalties payable in respect thereof. It is implicit here that the, obligations of the parties have been frozen in specific respects subject to the statutory exposition in this regard. However, the following judicial authorities, though with contrasting outcomes provides further insight on the contractual-regulatory dimensions of survival and sanctity of oil license agreements.

Firstly, under consideration is the case *Texaco Petroleum Company Limited and California Asiatic Oil Company V. The Government of Libya*, where the principle of sanctity of contract was considered in holding that the concession amounted to a binding obligation under International Law. Thus, the Libya Government was bound to honour its contractual undertakings. However, in the cases of *Libyan American Oil Company V. The Government of Libya* and *British Petroleum Company V. The Government of Libya*, the arbitrators relied on the existence of the New International Economic Order of May 1, 1974, a resolution favourably disposed to the sovereign rights of States to control and exercise ownership over their natural resources. Hence, the implication of the resolution, being to mitigate the expansive effects of the doctrine of sanctity of contracts, relative to natural resource concessionary arrangements.

## 6. CONCLUSION

Investments in Nigeria's upstream petroleum sector ought to be from a strategic perspective, subject to the enabling legislations. This necessitates informed manoeuvring to ensure positive and sustainable outcomes or returns. License fees and licensing regimes in the Nigerian upstream petroleum sector ought to be reviewed and renewed in conformity with the current contextual realities. Perhaps, contracting parties should be more innovative in deploying "freezing clauses" in licence agreements. This will help to manage losses attributable unilateral annulments, which is not uncommon to developing climes that rely heavily on oil revenues. Also important are issues of the enactment of a whistle blowers protection act, as such will promote increased transparency, and serve as a barometer to foster broader compliance levels. In addition, long over-due petroleum industry bill will complement the associated laws, rules, guidelines, codes, policies and initiatives in promoting operational efficiency and enhanced governance structures. These amongst other efforts at re-engineering Nigeria's oil and gas industry will foster accountability and healthy competition (Oyewunmi and Olujobi, 2016). It is also important to state that the effective harmonization of existing laws will help to mitigate regulatory overlaps and ensure improved consistency of issues on annulment and other related matters.

It is recommended that erring upstream petroleum companies should be blacklisted, and rules or guidelines must be designed to mitigate corrupt practices at the pre-qualification stage. The guidelines for pre-qualification and for tendering for oil licences ought to be advertised in not less than three national dailies. In addition, independent and non-partisan observers must be present in all the stages of the tendering from pre-qualification of companies, the bidding stage and the grant of contracts. Upstream petroleum companies bidding for petroleum licences or that maintain oil licences should duly disclose their actual titleholders. This probity and openness requirements may discharge public suspicious of government's officials of benefiting illegally from the award of oil licences and oil blocks. On a final note, the Federal government should set the tone by timeously publishing specifics of all licence annulments. This posture of reciprocal accountability will serve as a veritable benchmark to test the viability or otherwise of this option whilst also recognizing the importance of the wider societal corporate interest.

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