PROPOSAL FOR THE CREATION AND INCLUSION OF A 'RISK OIL CLAUSE' IN THE NIGERIAN PRODUCTION SHARING CONTRACT AS AN INCENTIVE TO ENCOURAGE INVESTORS TO EXPLORE FOR OIL IN NEW FIELDS*

Abstract

Production Sharing Contract is one of the ways in which a contractor, International Oil Company or perhaps an Investor as the case may be can acquire the right to explore for oil and produce hydrocarbon products in a particular given area. It is a contract that depicts a share of production between a National Oil Company or a Host Country and the Investor after all the necessary deductions have been made as agreed between them. One of the typical features of the PSC is that the risk of exploration is borne by the Investor and in an event that there is no finding, the Investor gets nothing for its trouble. However, if there is a finding, the Investor will recover its cost of investment in what is termed as the cost oil. It is common knowledge within the oil and gas industry that the more oil is produced, the shorter the life time of the reservoir, hence the need for the investor to continually search for other ways of oil production in order to balance its account record for its shareholders. This study makes a proposal for the creation and inclusion of a 'risk oil clause' in the Nigerian production sharing contract as an incentive to encourage investors to explore for oil in new fields.

Keywords: Production Sharing Contract, Energy Economics, Investors, oil and gas law

1. Introduction: Brief History of the Nigerian Oil and Gas Industry

The history of Nigerian petroleum can be traced as far back as 1908, when a 'German company, the Nigerian Bitumen Corporation, was attracted to what is now known as the South-Western Nigerian Tar Sand deposit'.[1] At that time, the exploration for oil in Nigeria commenced at a place very close to Okitipupa which is presently known as Ondo State. The exploration attempt was unsuccessful because the oil was not found in commercial quantity; however, it retains the record of being the pioneering effort for oil exploration in Nigeria.[2] More so, further activities of the German Bitumen Company completely stopped because of the First World War (1914-1919).[3] In 1937, Shell D'Arcy Petroleum Development Company of Nigeria again maintained the interest of the possibility of discovering oil in Nigeria. And this was backed up by the receipt of an Oil Exploration Licence (OEL) by Shell-BP in November 1938 which covered the entire country of Nigeria (357,000 square miles from the British colonial government).[4] Further exploration activities were interrupted as a result of the Second World War (1939-1945), after which the search for oil was continued by Shell-BP in 1946-1951. It has been said that in 1951 the first well that was drilled by Shell-BP was a dry hole. Efforts were concentrated in the Niger-Delta area of southern Nigeria for further four years without any success.[5] However, Shell-BP did not give up the search for oil and eventually found oil in commercial quantity (10000) barrels per day (bpd) in a place called Oloibiri, now Bayelsa State in the year 1956.[6]

A further discovery was made later in the year 1956 and in 1958, production of oil was at 5,100 bpd in which the first export of oil to Europe was made and that marked the entry of Nigeria into the international oil level.[7] It must be stated here that Shell-BP dominated the oil production in Nigeria due to lack of competitors and a 50-50 profit share formula was used between the Shell-BP and the Nigerian government.[8] Ever since oil was discovered in an economically viable quantity, exploration and production of oil has been sustained up till now largely in the Niger-Delta region of Nigeria.

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[1] Y Omorogbe, *Oil and Gas Law in Nigeria* (Malthouse Press Ltd, 2001).
[2]ibid.
[3] ibid.
[4] G Etikerentse, *Nigerian Petroleum Law (2nd ed.* Dredew Publishers, 2014).
[5]ibid.
[6] ibid.
[7] L Atsebgua, *Oil and Gas Law in Nigeria: Theory and Practice,* (Fifers Lane Publishers, 2013)
[8] G Etikerentse, (n 4).

From an initial output of 5,100 barrels per day in 1956, the Nigeria constantly moved to the sixth position on the Organisation of Petroleum Exporting Countries (OPEC) production chart.[9] This was because of the full participation of the government in the oil industry through its national oil company the Nigerian National Oil Company (NNOC) that was established in 1971.[10] In the month of July 1977, the NNOC and the Federal Ministry of Mines and Power merged together and the Nigerian National Petroleum Corporation (NNPC) was created. It can be said that oil is the main stay of the Nigerian economy and about one-fifth of the oil fields are offshore in the Niger-Delta area of southern Nigeria.[11] The proven oil reserves of Nigeria have been estimated by the U.S Energy Information Administration (EIA) be as much as 37.06 billion barrels.[12] In the time past, Nigeria provided some fiscal incentives to petroleum companies by reducing the petroleum tax to encourage exploration especially in the deep waters.[13]

By way of summary, oil production in Nigeria began about seventy years ago after the preliminary search for the oil began. After that period, there has been steady growth in the production of the oil and newer means in strengthening its laws, policies and means of acquisition of oil rights in the industry especially through its national oil company.

2. Acquisition of Oil Rights in Nigeria

There are various ways in which an oil company desiring to explore for oil in a country can acquire such rights. They can be in form of constitutional provisions, laws, regulations or contractual arrangements.[14] In terms of acquisition of oil rights through the constitution, the constitution will normally give its government the power to create and to provide laws in its country. In most cases, it addresses the issue of ownership of the natural resources of the country. It always vests the entire ownership of the natural resources which includes the oil and gas of the country on the government of that country, a typical example of this provision is section 44(3) of the 1999 Constitution of the Federal Republic of Nigeria (as amended) which vests ownership and control of the all-natural resources in the country on the federal government of Nigeria. In terms of the laws and regulations, a designated law is provided to govern the oil and gas activities in terms of rights and duties of the parties involved. A typical example of this is the Nigerian Petroleum Act of 1969. There are also other laws that can also support the main legislation in terms if regulations governing the for-example health and safety, environmental regulations, taxes, pipelines etc.[15] An example of this law in Nigeria is the National Environmental Standards and Regulations Enforcement Agency 2007 (NESREA) which regulates the protection of the environment.

The last but very popular means of acquisition of oil rights in the oil and gas industry is through contractual arrangements such as concession, production sharing contract (PSC), service contract and joint ventures. These contracts define the rights and duties of the parties to the contract. A concession arrangement grants to an international oil company IOC proprietary rights over the specified contract area a total ownership of all oil and gas that it successfully produces, subject to the payment of a royalty as well as income tax (they all vary in accordance to the size of production).[16] In other words, it can be said that typically under a concession, the contractor is seen as the owner of the oil *in situ*.
Product Sharing Contracts as well as service contracts do not vest ownership of the oil in the ground on the contractor. While under the PSC, the contractor is only entitled to the percentage share of its production, under the service contract, the contractor normally receives a fixed fee for its service of extracting the oil if found.[17]

[9] https://www.opec.org/opec_web/en/about_us/167.htm. Accessed 10/08/2020 at 23:29.
[10] G Etikerentse, (n 4).
[11] G Etikerentse, (n 4).
[12] (https://www.eia.gov accessed 10/08/2020).
[13] G Etikerentse, (n 4).
[14] J West, *Oil Contracts: How to Read and Understand them*, (Petroleum Economist, the Authority on Energy, 2012).
[15] ibid.
[16] Allen & Overy, Guide to Extractive Industries Documents – Oil & Gas World Bank Institute Governance for Extractive Industries Programme September 2013. www.allenovery.com Accessed 20/02/2021.
[17] J West, *Oil Contracts: How to Read and Understand them*, (Petroleum Economist, the Authority on Energy, 2012).

Joint venture is also an arrangement that can be used alongside the other types of arrangements like the PSC, concession or a service contract. It has been said that this in the real sense is not an 'alternative' to the PSC model. In a joint venture, the IOC or the contractor and the State come together and 'jointly participate in the exploration and development' oil and gas. In this arrangement, the host country will them be entitled to a share of the profits as a participant, which also include other financial benefits in the form of profit oil, royalties, taxes); 'accordingly, the State is required to contribute to the costs of operating and development, unless it takes a 'carried' interest').[18]

Having understood the various ways in which a contractor can acquire rights to produce oil and gas in a given area, it is pertinent at this juncture to bring out the modes of acquisition of rights in Nigeria. It can be said that the early form of acquisition of oil rights in Nigeria was through concession which had some peculiar features. The concession was for a very large area which was extended over the whole country and it was for a very long time which was between 40 -75years.[19] The contract was often granted an exclusive and extensive rights over all the mineral deposits in the area and was at liberty to dispose of them as it deemed fit. The financial benefits accruing to the host states were usually ridiculous. In most cases the contractors paid a nominal rent of $150 and a bottle of rum for a whole concession and the royalties that were paid were based on volume of output, rather than value.[20] It can be seen that these features were clearly unjust and was tilted in favour of the contractors. The concession in Nigeria and other developing countries that had the same experience as discredited this form of contractual arrangements as 'the very word 'concession' has a bad connotation in many countries'.[21]

The prejudices against concession are drawn from the above main features which are peculiar to the concession, than from the general features of the contract type. 'In fact, concessions thrive all over the world today in a modernised form and often with a different name (licence, permit, lease it agreement)'.[22] There are two main ways of acquisition of oil rights in Nigeria. The first one is through a licence under the Petroleum Act, 1969 now CAP. P 10 (LFN) 2004 and the second one is through PSC. A license has been defined to be a permission to do an act which without such permission would be illegal.[23] Section 2 of the Petroleum Act provides that 'subject to this Act, the Minister may grant *(a)* a licence, to be known as an oil exploration licence, to explore for petroleum; *(b)* a licence, to be known as an oil prospecting licence, to prospect for petroleum; and *(c)* a lease, to be known as an oil mining lease, to search for, win, work, carry away and dispose of petroleum. (2) A licence or lease under this section may be granted only to a company incorporated in Nigeria under the Companies and Allied Matters Act or any corresponding law'.

Production Sharing Contract was first introduced in Indonesia in the year 1966.[24] In a PSC, the host country enters into a contractual arrangement with a contractor which can also be an indigenous or other state's national oil company.[25] In this type of arrangement, the contractor will agree to make provisions for both the financial aspect as well as the technical know-how for the exploration and production of the oil and gas.[26] It is always the case that the host country be represented by its national oil company (NOC), who has the responsibility to take 'delivery of the State's share of production'.[27] The contractor will normally be 'granted an exclusive right to explore and produce oil and gas within a defined area (generally known as the contract area)'. It is important to take note that the contractor solely bears the whole risk of the cost of exploration, production, financial etc. In an event that an economical viable discovery is declared, the contractor then recoups its costs of investment by taking a portion of the oil to serve as 'payment' for its efforts '(generally at the end of the quarter in which the oil is produced)'.

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[18] Allen & Overy, (n 16).
[19] Y (Omorogbe, (n 1).
[20] Y Omorogbe, 2001 (n 1).
[21] Y Omorogbe, 2001 (n 1).
[22] Y Omorogbe, 2001 (n 1).
[23] G Etikerentse, (n 4).
[24] P Roberts, 'Production Sharing Contract: the Indonesian Experience' (1998) 1 O.G.L.R 10.
[25] Allen & Overy, (n 16).
[26] Allen & Overy, (n 16).
[27] Allen & Overy, (n 16).

[28]And the remainder of the oil is shared between the host country and the contractor in predetermined proportion.[29] It must also be stated here that in an event that no discovery is made, the contractor gets nothing for its trouble and the State remains the owner of the oil at all times where discovery is made in commercial quantity which can only be subject to the cost recovery of the contractor.[30]

3. Industry Players in Nigeria: the Wheel beneath their Drive

It is a known fact that Nigeria is one of the oil giants in Africa and as such a lot of significant international oil companies (IOCs) operate in Nigeria. IOCs such as Petrobras of Brazil, AGIP, Shell, Nexen, a Chinese Company, Total, Statoil, a Norwegian Oil Company, Chevron of USA, Mobil, Exxon Mobil, ENI. (OilGasNg.Com). All these and others have been operating in Nigeria for many decades. It has been reported that Nigeria been rated very high in terms of oil and gas reserves.[31] Accordingly, Nigeria has been reported to be one of the largest 'oil producer in Africa with proven geology, and long-established infrastructure, regulatory and fiscal regimes'.[32] Nigeria is also known as one of the homes of the largest gas reserves on the continent of Africa, in the development of it can be seen as a lucrative source of growth of its domestic and international markets. It has been sad that 'Nigeria's oil and gas industry represents a compelling value proposition and is attractive to oil companies. Especially the hydrocarbon geology of the Niger Delta area, where Nigeria's oil and gas industry is concentrated'.[33] Another reason why Nigeria is an attractive place of investment to oil companies is the fact that the crude oil has low sulphur which implies that less refining will be needed when processed.[34] It can also be said that Nigeria has a favourable fiscal regime to the international oil companies. While there are adequate laws protecting the environment and other health and safety procedures, the implementation of these are always very relaxed. Thus, oil companies are do not always have to be worried about being caught up with all these issues. While this is not a plausible idea for the host country, it is true that all these do happen, and it should not be a sustainable reason for either of the parties involved.

4. Nature of Production Sharing Contract

As it has already been established, under a PSC, a state or a host country enters into an agreement or a contract with an investor or international oil company (IOC) international for the investor or IOC to provide all the necessary finance, labour as well as technical expertise in order to explore for and if found produce oil and/or gas.[35] It is said here that the host country will normally be represented by its national oil company (NOC) or any designated body of the government. In that light, the investor under the agreement will be given an exclusive right to explore and if found, produce oil and gas within the allocated area (which can be referred to as the as the contract area.[36] It must also be mentioned here that the investor solely bears the whole risk of the project. Should a commercial discovery be declared, the IOC becomes entitled to a portion of any oil produced as 'payment' for its efforts (generally at the end of the quarter in which the oil is produced), in addition to recouping its costs out of production; conversely, if no discoveries are made, the IOC receives nothing. The State retains ownership of all oil and/or gas produced (subject only to the IOC's entitlement to a portion of any oil produced on a successful discovery). The extent to which the NOC is involved with the exploration and production process varies from country to country.[37] From the host country view, the glaring merit of 'the PSC model is the minimal risk on its part; it is able to reap the benefits of its natural resources without having to spend its own time and money'.[38] It is usually considered that the host country may likely not have the technical know-how that will be needed for the exploration and production of oil and/or gas and by this consideration, the assistance of the experienced investor will be relied on for the exploitation of the oil and gas.

[28] Allen & Overy, (n 16).
[29] Allen & Overy, (n 16).
[30] Y Omorogbe, 2001 (n 1).
[31]Seplat Petroleum Development Company, 2018 https://seplatpetroleum.com. Accessed on 26/08/2020.
[32] Vanguard https://www.vanguardngr.com/2018/03/seplat-rates-nigeria-high-oil-gas-reserves. Accessed 26/08/2019.
[33] Seplat Petroleum Development Company, 2018 (n 31).
[34] L Atsebgua, (n 7).
[35] Allen & Overy, (n 16).
[36] Allen & Overy, (n 16).
[37] Allen & Overy, (n 16).
[38] Allen & Overy, (n 16).

Main Features of the Production Sharing Contract

While there are different forms in which PSC can be drafted which is dependent on what it is for and the particular peculiarity of the country, there are certain features that are commonly found across all PSCs. These features are key to any well drafted PSC. It is to this, that a brief discussion will be made here.

Royalty Oil:

When oil is discovered, usually the first thing that the investor will pay the host country is a royalty. This royalty is always paid on gross production to the host country or the state. The royalty can be paid either in cash or in kind (a production share of the oil being proportional to the price).[39]

Cost oil:

Next to the payment after royalty is the payment of what is referred to as 'cost oil' which is investor is allowed as his entitlement a certain percentage on the production which has already been pre-determined by the parties to the PSC. This percentage on production serves as cost of its investment. The cost oil is usually paid over a specific time agreed by the parties in which costs can be carried forward until it is fully recovered and paid.[40]

Profit oil:

After the royalty and cost oil have been deducted, the oil that is left is called the 'profit oil'. The profit oil is shared between the investor and the state in consonance with the PSC. It must be mentioned here that the percentage share of the state will normally increase as just as production.[41]

Income tax:

The next important common feature of the PSC is the 'income tax'. It is always the practice that the investor will be made to pay tax on its share of its profit oil. It is to be known as the income tax is usually paid by the states national oil company or the state on behalf of the IOC.[42]

Littoral States and the Potential Oil and Gas Areas in Nigeria

Nigeria is comprised of thirty (36) states that make up the Federation of Nigeria. Below is the map of Nigeria:

[39] C Duval, Leuch, Le. Pertuzio, H. Weaver, J. A. (2nd ed) 2009 *International Petroleum Exploration and Exploitation Agreements: Legal, Economic and Policy Aspects* New York: Barrows, 2009 10.

[40] Ahmadov, I., Artemyev, A., Aslanly, K., Rzaev, I., Shaban, I., 'How to scrutinise a Production Sharing Agreement: A guide for the oil and gas sector based on experience from the Caspian region International Institute for Environment and Development' (2012) (www.pubs.iied.org/pdfs/163031IIED.pdf last visited January 19th, 2020).

[41] Allen & Overy, (n 16).

[42] P D Cameron, *International Energy Investment Law: The Pursuit of Stability (*Oxford: Oxford University Press, 2010).

Figure 1: The Map of Nigeria showing the Littoral States.[43]

Out of the 36 states, there are nine (9) states that produce oil and gas which differs in production quantity. All the oil producing states are in the south and western part of the Nigeria. At the top is Akwa Ibom State with the production of 504,000 barrels per day (bpd)., followed by Delta State at the second position with the production of 346,000 bpd, followed by Rivers State with the production of 344,000 bpd, followed by Bayelsa State with the production of capacity of 290,000 bpd, followed by Ondo State with the production of 60,000 bpd, followed by Lagos State with the production capacity of 40,000 bpd, followed by Edo State with the production capacity of 33,000 bpd, at the 8th position is Imo State with the production capacity of 17,000 bpd and lastly at the 9th position is Abia State with the production capacity of 11,000 bpd.[44] Below is a diagram showing the various states and the level of oil production from each states.

[43]https://www.google.com.ng/search?q=the+map+of+nigeria&client=ms-android-samsung&prmd=imnv&source=lnms&tbm=isch&sa=X&ved=0ahUKEwj9tvjjhc3dAhUpLsAKHaukD7kQ_AUIESgB&biw=412&bih=766&dpr=2.63#imgrc=UOH853lnGiPOQM:&isa=y accessed 21/09/2019.
[44] https://infoguidenigeria.com/oil-producing-states/. Accessed 21/09/2019

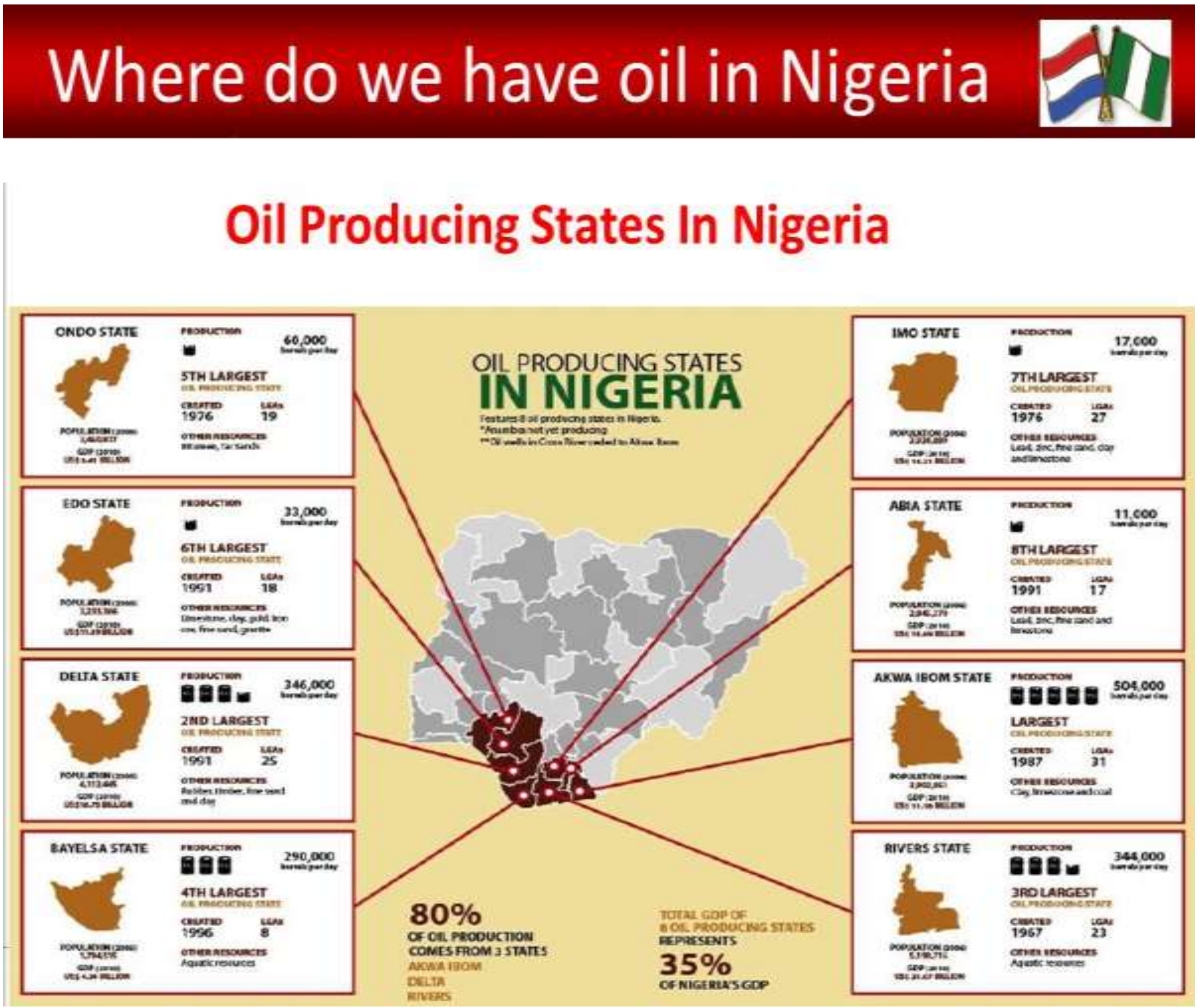

Figure 2: Oil Producing States in Nigeria[45]

The Nigerian National Petroleum Corporation (NNPC) being the national oil company (NOC) of Nigeria has announced that there is a potential that oil can be discovered from the northern part of the country. This was informed on the fact that 'discoveries made in neighbouring countries in basins with similar structural settings which covers also the Yola, Sokoto Basins and also the Middle/Lower Benue Trough all of northern Nigeria.[46]

Impediments to Oil Exploration and Production in Nigeria

Nigeria's oil and gas industry is to a large extent controlled by the government owned NNPC where joint ventures (JVs) and PSCs with IOCs. There are quite several impediments to oil exploration and production in Nigeria which can raise concerns to oil and gas investors. It has been reported by KPMG 'that the process of contract award in the Nigerian oil and gas upstream sector is "tedious and lengthy". The report stated that the duration of contract award between the initiation and eventual execution of an agreement can take as long as 36 months'.[47] This has a tendency of affecting the economics of any project contract. Investors that desire to invest in Nigeria should keep this in mind and find a way to begin the process of the award of any potential contract before the project commences. It has also been reported that one of the persistent problems in Nigeria's oil and gas sector is the failure of the NNPC to honour its cash call duties to joint venture which as a result leave investor with a challenge of making good the default.[48] Apart from the above impediments there are other pressing problems associated with

[45] www.sankey-diagrams.com/nigeria-oil-production-2013/ accessed 21/09/2020.
[46] NNPC intensifies Oil Search in Benue Trough. See nnpcgroup.com accessed 02/04/2020.
[47]Rigzone, https://www.rigzone.com/news/oil_gas/a/140046/the_strengths_challenges_of_investing_in_nigeria/.Accessed 16/10/2020.
[48] G Etikerentse, Nigerian *Petroleum Law (*Dredew Publishers, 2nd ed. 2014).

the oil exploration and production in Nigeria which has to do with corruption, theft and pipelines vandalization,[49] although efforts have been put forward to suppress these issues.

5. Risk Oil Clause in the Production Sharing Contract in Nigeria

In order to encourage the investors to explore for oil in seemingly potential areas in Nigeria, it is the proposal of this chapter to put forward a risk oil clause in the fiscal regime in the PSC. Before then, the fiscal regime applicable in Nigeria will be briefly discussed while laying the foundation for the risk oil clause. The government perspective as well as the investors' perspective will be discussed in order while eliciting the advantages and disadvantages from their perspectives. After the discussion, there will also be a section that will try to find the balance as a result of the inclusion of the risk oil in the PSA.

Fiscal Regime in the Production Sharing Contract in Nigeria

The Petroleum Profit Tax Act (PPTA)[50] is the piece of legislation in Nigeria that governs the taxes in the oil and gas sector. Other corporations in Nigeria are generally taxed under the Companies Income Tax Act, 1990.

> The PPTA provides for the collection of tax imposed on the profits made from petroleum operations. The Act is meant to apply to the taxation of the assessed income profits of companies engaged in petroleum operations, be it crude oil or natural gas. It contains provisions relating to the definition of the operations of companies that are subject to the Act. It also defines factors to be considered in calculating tax payable by any affected company with provisions for effecting petroleum profits tax payment.

Section 8 of the PPTA that 'there shall be levied upon the profits of each accounting period of any company engaged in petroleum operations during that period a tax charged, assessed and payable in accordance with the provisions of the Act." The rate of tax payable to the Federal Government of Nigeria by the investor under the PPTA in any PSA is 85%. Royalty oil is also paid to the owner of the resources which is the Nigerian government. The royalty is paid in accordance with the location of the production site. As such, the deeper the location of the drilling the lower the royalty rate and vice versa.[51] The payment of PSC royalties in Nigeria are provided for in section 5 of the Deep Offshore and Inland Basin Production Sharing Contracts Act 1999 No 9 and the 'Petroleum (Drilling and Production) (Amendment) Regulations 2003 for onshore and shallow offshore areas'.[52] The royalties in Nigeria are payable on volume and decreases as the water depth deepens. They are currently as follows:

Areas	Water depths in Metres	Royalty payable in %
Onshore	Not applicable	20%
Offshore	0-100 metres	18.5%
Offshore	100-200 metres	16.67%
Offshore	210-500 metres	12.00%
Offshore	501-800 metres	8.00%
Offshore	801-1000 metres	4.00%
Offshore	> 1000 metres	0%

Table 1[53]

The cost of exploration and production is recoverable by the investor in an event of a commercial discovery. The cost oil is negotiated in agreed terms between the parties. Usually the cost oil is not totally recoverable in the first year of production to allow some benefits to be enjoyed by the host

[49] Rigzone https://www.rigzone.com/news/oil_gas/a/140046/the_strengths_challenges_of_investing_in_nigeria/. Accessed 16/10/2020.
[50] Cap 60, Laws of the Federation of Nigeria, 1990
[51] G Etikerentse, Nigerian *Petroleum Law (*Dredew Publishers, 2nd ed. 2014).
[52] ibid.
[53] Y Omorogbe, *Oil and Gas Law in Nigeria* (Malthouse Press Ltd, 2001).

country. It is usually recoverable in the first few years of production. For example, it 'was fixed at 40% of crude oil production and later revised to 50% in 1986 (made retroactive from April 1977) in respect of the NNPC/AON PSC.'[54] As previously stated, profit oil is the available oil after the deduction of the royalty oil, tax oil and cost oil. The profit oil is then shared between the parties in accordance with the terms or arrangement of the PSC. Under the PSC between NNPC/AON, 'the percentage was fixed at about 45% out of which NNPC received 65%, while that of AON was 35% with a proviso that when daily production reached a minimum level of 50,000 barrels, the NNPC's share would be increased to 70%.'[55] The PSCs after the year 1993, 'profit oil is shared between the NNPC and the contractor at varying levels of production; favouring the Investor at lower levels and gradually shifting NNPC's favour as production increases'. There are also bonuses payable to the host state by the Investor (signature and production bonuses as well as Memorandum of Understanding).[56]

Risk oil Clause in the Production Sharing Contract in Nigeria

There are quite a number of incentives available to the oil and gas investors to encourage them to explore for more oil in Nigeria. The 85% tax by the PPTA on oil and gas is seen to be quite on the high side from the investors' perspective. In a bid to make it attractive, other incentives have been in place for the Investors benefit. Several fiscal reliefs in the PPTA have been put forward to ameliorate to a reasonable degree the impact of the seemingly high tax rate of 85%. The fiscal reliefs are in the form of tax relief exemption. This has been done in order to increase the investor's profit margin.[57] It is important to highlight the fiscal incentives available to the Investors in Nigeria before discussing the risk oil clause as proposed in this final report. The several incentives in the PSCs executed in 1993 were approved under the Nigerian Government and passed into law the agreed fiscal terms, which are now contained in the Deep Offshore and Inland Basin Production Sharing Contracts Act 1990 No. 9, are as follows:

i. The petroleum profits tax applicable under the PSCs shall be determined in accordance with the PPTA, provided that the petroleum profits tax applicable shall be 50 percent flat rate of the chargeable profits for the duration of the PSC (section 3(1) of the PPTA).

ii. Where the NNPC- the holder of the licence and the other party to the PSC, the Contractor, have incurred any qualifying capital expenditure wholly, exclusively and necessarily for the purposes of petroleum operations under the PSC in the Deep Offshore or Inland Basin, there shall be due to the parties in respect of PSCs executed prior to July, 1998 a credit (referred to in the Act as 'Investment Tax Credit') at a flat rate of 50% of the qualifying expenditure in accordance with the PSC terms for the accounting period in which the asset was first used. However, in respect of parties who executed PSCs after July 1, 1998, there shall be to them an allowance (referred to in the Act as 'Investment Tax Allowance') at a rate of 50 percent of the qualifying expenditure in accordance with the provisions of existing applicable legislation for the accounting period in which the asset was first used.[58]

Section 5 provides that the following royalty rates shall apply to the Deep Offshore Production Sharing Contracts.

a. In areas from 201 to 500 metres water depth …………….12%
b. from 501 to 800 metres water depth ………………………8%
c. from 801 to 1000 metres water depth …………………… .4%
d. in areas in excess of 1000 metres water depth …………….0%
e. in Inland Basin areas……………………………………….10%

i. Section 11 of 1999 No. 30 which amends section 20 of the PPTA provides as follows:
    a. a company which executed a PSC in 1993 with the NNPC shall throughout the life of the PSC be entitled to claim an investment tax credit allowance as an offset against tax in accordance with the provisions of the PSC.
    b. the investment tax credit rate applicable to the contract area shall be fifty percent flat rate of chargeable profit for the duration of the PSC.

[54] G Etikerentse, Nigerian *Petroleum Law (*Dredew Publishers, 2nd ed. 2014).
[55] L Atsebgua, *Oil and Gas Law in Nigeria: Theory and Practice,* (Fifers Lane Publishers, 2013).
[56] G Etikerentse, Nigerian *Petroleum Law (*Dredew Publishers, 2nd ed. 2014).
[57] Y Omorogbe, *Oil and Gas Law in Nigeria* (Malthouse Press Ltd, 2001).
[58] see section 4(1) of 1999 No. 9 and section 11 of 1999 No. 30-the latter amending section 20 of the PPTA.

c. in computing the tax payable investment tax credit shall be applicable in full to petroleum operations in the contract area such that the chargeable tax is the amount of the assessable tax less the investment tax credit.

d. The chargeable tax computed under (c) in the foregoing shall be split between the parties in the proportion of the percentage of profit oil split.

For the royalty rates for the PSC onshore and shallow offshore areas, an amendment to the petroleum (Drilling and Production) Regulations contained in Statutory Instrument No 6 of 2003 (now Regulation 60C- Petroleum (Drilling and Production) Regulations) the following are stipulated as the royalties effective January 1, 2000 for PSCs' onshore and shallow offshore production.

a. Onshore-
i. for production below 2 thousand barrels of oil per day…………5.0%
ii. for production below 2 and 5 thousand barrels of oil per day…...7.5%
iii. for production below 5 and 10 thousand barrels of oil per day….15.0%
iv. for production above 10 thousand barrels of oil per day…………20%
b. offshore up to water depth of 100 metres-
i. for production below 5 thousand barrels of oil per day………….1.5%
ii. for production below 5 and 10 thousand barrels of oil per day….7.5%
iii. for production below 10 and 15 thousand barrels of oil per day…12. 5.0%
iv. for production below 15 thousand barrels of oil per day………….18.5%
c. offshore between water depth of 100 and 200 metres-
i. for production below 5 thousand barrels of oil per day………….1.5%
ii. for production below 5 and 10 thousand barrels of oil per day….3.0%
iii. for production below 10 and 15 thousand barrels of oil per day…5.0%
iv. for production below 15 and 25 thousand barrels of oil per day…10%
v. for production above 25 thousand barrels of oil per day…………16.67%.[59]

As stated in chapter one of this final report, the risk oil is proposed is a percentage of the total cost oil and should be couched as follows 'the parties to this PSC have agreed that a % of the total cost oil be recoverable by the investor as risk oil'. In other words, whatever cost oil earmarked for the investor as the cost of exploration and production, a percentage of such cost oil should be recoverable by the investor to be known as the risk oil. This incentive is provided even before exploration begins and it is quite different from other incentives which are provided in the course of production. It is the believe of this final report that the exploration for oil and gas is more like a gamble as there is never certainty of discovery of oil however promising the geophysical surveys are. The risks of the investors are always enormous and, in an event that there is no finding, all the risks of investment is lost without any obligation on the host state. Where oil is found, it is the proposal of this article that there should be more than just cost oil and profit oil accruable to the investors but also a 'risk oil' which should be half of the total cost oil. The argument here is that since investor gets nothing if oil is not found then the investor should get something more than only the cost of investment and the its share of the profit oil.

6. Conclusion

It is gathered here that from the perspective of the government, the incentive in form of the risk oil should be restricted only to new fields. Where oil is found, the risk oil can be recoverable over the years. It is proposed here that the risk oil be recovered in succession of the cost oil. It can also be said that from the investors' perspective, it may not be seen as much of an incentive as a motivation than an increased share of the profit oil. This can be viewed from the stand point of the fact that the risk oil is a one-time incentive which will come to an end when it is fully recovered unlike a higher percentage share of the profit oil that can last the life time of the contract. To counter this, the risk oil is an additional incentive to the numerous incentives already in place in the PSC in Nigeria including favourable profit margins. It should be a known fact that the more cost accrued by the investor the less tax is paid.

[59] G Etikerentse, Nigerian *Petroleum Law (*Dredew Publishers, 2nd ed. 2014).