**Nigeria’s Petroleum Industry Act: Addressing old problems, creating new ones**

Earlier this year Nigerian President Muhammadu Buhari signed the [Petroleum Industry Act (PIA) 2021](http://www.petroleumindustrybill.com/2021/09/01/the-official-gazette-of-the-petroleum-industry-act-2021/#.YVIJQLhKhPY), bringing to a close a 20-year effort to reform Nigeria’s oil and gas sector, with the aim of creating an environment more conducive for growth of the sector and addressing legitimate grievances of communities most impacted by extractive industries.

A lot has changed in the sector domestically and globally since the reform efforts began. The number of indigenous oil and gas firms has grown, but so has the number of oil-producing countries in the region. Militancy in oil-rich communities, while remaining, has diminished. Concerns over climate change have fueled aggressive efforts to reduce global consumption of fossil fuels—driving [divestment](https://www.washingtonpost.com/education/2021/09/10/harvard-divest-fossil-fuels/) from oil and gas by companies, [institutions](https://www.bu.edu/articles/2021/boston-university-divest-from-fossil-fuel-industry/#:~:text=Boston%20University%20will%20divest%20from,of%20campus%20activism%20and%20protests.), and [countries](https://www.eia.gov/todayinenergy/detail.php?id=48596#:~:text=Coal%20accounted%20for%2013%25%20of,electricity%20and%20heat%20in%202020.).

The PIA represents an effort by Africa’s leading oil-producing country to respond to this changing environment. In 2019, the oil and gas sector accounted for about [5.8 percent of Nigeria’s real GDP](https://www.nigerianstat.gov.ng/pdfuploads/GDP_Report_Q2_2020.pdf) and was responsible for 95 percent of Nigeria’s foreign exchange earnings and 80 percent of its budget revenues. In addition, because the law is far-reaching in its remit, it is complex and not easy to summarize.

If properly and vigorously implemented, the PIA can represent the gold standard of natural resource management, with clear and separate roles for the subsectors of the industry; the existence of a commercially-oriented and profit-driven national petroleum company; the codification of transparency, good governance, and accountability in the administration of the petroleum resources of Nigeria; the economic and social development of host communities; environmental remediation; and a business environment conducive for oil and gas operations to thrive in the country. However, these results are conditional on Nigeria’s political and oil industry leaders overcoming some key challenges that are discussed following the summary of the key provisions of the act.

**Key provisions/innovations of the act**

**A new regulatory and governance architecture**

The PIA overhauls the regulation and governance of the oil and gas industry. The law provides for two regulatory agencies—the Nigerian Upstream Petroleum Regulatory Commission (NUPRC) and the Nigerian Midstream and Downstream Petroleum Regulatory Authority, (NMDPRA)—that will be responsible for the technical and commercial regulation of petroleum operations in their respective sectors, and have the power to acquire, hold, and dispose of property, as well as sue and be sued in their own name.

The law commercializes the perennially loss-making state-owned enterprise, the Nigerian National Petroleum Company (NNPC), turning it into the NNPC Ltd, a quasi-commercial entity the ownership of which shares shall be vested with the government, and the ministries of Finance and Petroleum shall hold the shares on behalf of the government. Per the PIA, the president of Nigeria will appoint the president of NNPC Ltd as well as heads and members of the regulatory agencies. Separately, the minister of petroleum, then, will head the industry with a wide range of powers to formulate, monitor, and administer government policy under the PIA.

Importantly, the PIA provides that 30 percent of the profits of the NNPC Ltd will fund a new entity, to finance exploration in other basins in the country (Frontier Exploration Fund). Ten percent of rents on petroleum prospecting licenses and 10 percent of rents on petroleum mining leases are also assigned to Frontier exploration. The act is unclear on whether there will continue to be exploration in existing basins.

**A new era for host communities?**

The relationship [between oil and gas host](https://reliefweb.int/report/burkina-faso/irin-update-977-events-west-africa) communities in Nigeria has historically been very poor. The PIA aims to address this problem by creating the Host Community Development Trust Fund (HCDTF) whose purpose will be to, among others, foster sustainable prosperity, provide direct social and economic benefits from petroleum to host communities, and enhance peaceful and harmonious coexistence between licensees or lessees and host communities. Specifically, the law stipulates that existing host community projects must be transferred to the HCDTF, and each settlor (or oil license holder) must make an annual contribution of an amount equal to 3 percent of its operating expenditure for the relevant operations from the previous year. The management committee of the trust must include one member of the host community. In addition, the act stipulates a penalty for failure to comply with host community obligations, including revocation of license.

Interestingly, the PIA also imposes the [duty and responsibility](https://bracewell.cld.bz/Understanding-Nigerias-PIA) to protect oil and gas assets on host communities. More specifically, clause 257 stipulates that any host community that fails to protect oil assets in its community from vandalism will be held accountable for the repairs.

A persistent concern for host communities is the continued degradation of their environment and habitat from gas flaring associated with oil drilling. Nigeria has passed several laws to stop this with little effect. The PIA penalizes companies for gas flaring and provides that the revenues from the penalties will be used for environmental remediation and relief of the impacted host communities. However, the penalty must be steep enough to achieve its intended purpose. If it is not, oil companies will continue to flare gas if doing so minimizes their cost more than the penalty adds to it.

**A new fiscal framework**

The PIA introduces a new tax regime, replacing the existing petroleum profits tax with a **hydrocarbon tax** and introducing a tax on the income of oil companies. Under this new fiscal regime, hydrocarbons—including crude oil, condensates, and natural gas liquids produced from associated gas—will be subject to taxation. Notably, crude oil from deep offshore is excluded from the tax.

One of the more controversial stipulations in the PIA is the provision stating that, in the event of supply shortfalls, only companies with active refining licenses or proven track record of international crude oil and petroleum products trading will be allowed to import such products. This is a controversial provision that has been interpreted as an attempt to confer monopoly powers on a few domestic refiners.

Finally, the fiscal framework provides for penalties for gas flaring arising from midstream operations. Revenues from these penalties will accrue to the Midstream and Downstream Infrastructure Fund and will be used to finance midstream and downstream infrastructure investment.

**Challenges**

**Ambiguous and imprecise language.** The most important challenge is the challenge of interpretation and imprecisions in the law. For example, it is unclear whether host community development trust obligations are additional to existing community levies (such as the Niger Delta development levy) or will be an aggregation of those levies. Similarly, the law is silent on the definition of “frontier basin” and host community, instead deferring to the NUPRC on the definition of frontier basin and to settlors or license holders on the definition of “host community.” These definitions are not neutral to revenue; they have revenue implications. This lack of clarity creates uncertainty and even possible disputes, especially if relevant parties define them differently.

**Capacity building.** This law is complex and complicated. While capacity in the oil and gas sector has been built over the years, the new legal provisions and fiscal framework will need new capacities to succeed. This challenge will be particularly acute in the new regulatory institutions; in the understanding, interpretation, and application of the law; and in the management of the funds, including the HCDTF.

**Lingering North/South disagreement.**The bill that became the PIA was originally proposed by the executive (largely supported in the North) and passed largely along regional (North/South) lines. In short, lawmakers and leading politicians from the oil-rich [Niger Delta states opposed it](https://www.vanguardngr.com/2021/08/niger-delta-stakeholders-reject-pib/), and many lawmakers from the South believe the bill advances Northern interests to the detriment of the South.

In fact, although enacted, the PIA continues to generate anger in the Niger Delta region. For example, critics of the PIA claim the 3 percent contribution to HCDTF is insufficient and the 30 percent profit to the NNPC Ltd for the Frontier Basin Development Fund unfair. Suspicions in the South that the Frontiers Basin Fund is a means of transferring resources to the North have been given credence by public statements by some Northern leaders. For example, the Group Managing Director of NNPC, a Northerner, recently stated that the North [will benefit more from the law](https://gazettengr.com/north-will-benefit-more-from-pia-nnpc-gmd-kyari/) because “new crude oil deposits are being discovered in the region and the funds derivable from exploration would propel more discoveries in the North.”  Such statements hurt efforts to arrive at a national consensus on oil and gas policy that is region neutral in its interpretation and that is in the interest of the country. There is, thus, a very serious challenge of building a national consensus for the law without which some of the objectives of the law may not be achieved.

**Tensions over revenue sharing.** The law has serious implications for the **public finances of the federation and its constituent states and local government areas.** First, the reduction in taxes and royalties will result in considerable reduction in revenues to the three tiers of government at a time they cannot afford it. Second, Nigeria’s revenue law requires that entities or enterprises owned by the federation remit their profits to a pool, the Federation Account, for sharing among the three tiers of government. Revenue from the Federation Account accounts for more than 80 percent of the revenues of many states and local governments. Therefore, the stipulation that 30 percent of NNPC Ltd.’s profits must be set aside for frontier exploration could cause a significant decrease in its contribution to the Federation Account. In the short term, revenues shared among the three tiers of government from the Federation Account will fall. Many states and local governments, especially those with very weak internal revenue-generation capacity will be unable to discharge their duties of providing essential social services to their citizens. Then again, such a change could lead to innovations at the state and local government levels to increase internal revenue-generating capacity and fiscal efficiency, such that the long-term effect of this policy could be positive.

Host communities remain unhappy with the PIA’s provision that oil companies must allocate 3 percent of their annual operating expenditure in the immediately preceding calendar year to the HCDTF; they had asked for 10 percent.

Furthermore, now that most onshore oil wells are owned by indigenous oil companies, host communities are uncertain whether this contribution will be even made. The previous owners of the oil wells were foreign companies, meaning that there were two sets of laws—Nigerian and those of the home country—to apply pressure for legal compliance. Now, with domestic ownership of most onshore oil wells, the risk of noncompliance with host community contributions is high, especially since, in Nigeria, the risk of political and regulatory capture of the new industry governance institutions is high, the judiciary is weak, and court decisions are seldom enforced. The domination of onshore oil activities by indigenous companies raises legitimate fears that no contributions will be made to the HCDTF, which means that host communities will remain underdeveloped. Related, a particularly sticky provision of the law is the stipulation of punishment for host communities for acts of vandalism of oil assets committed in their domain. This provision imposes collective punishment on host communities for acts of vandalism that they may not have committed and could raise constitutional and legal problems for the PIA.

The PIA also comes with a challenge of equity between **indigenous oil producers and multinational corporations.** International producers such as Shell have largely disengaged from onshore oil exploration and production activities, concentrating instead on deep offshore. As stated earlier, deep offshore is exempt from taxation. By divesting themselves of onshore assets, international multinationals are “technically” exempt from the 3 percent contribution to the HCDTF. These provisions confer cost advantages to oil multinationals, making it difficult for indigenous companies to compete and grow. One solution might be to amend the act to require all oil companies operating in Nigeria to contribute to the HCDTF.

**Politics.** Under the PIA, the president has the power to appoint members of the boards of the various institutions established by the act. Appointments to the boards of oil companies are watched keenly and could be a source of discontent among constituent parts of the country. To manage this discontent, it has become the norm (but is not the law) to have at least six positions in the board of federally owned companies and parastatals, reflecting the six geopolitical zones of the country. Unfortunately, the PIA does not create enough board positions for this condition to be met. Not increasing the number of board positions to manage out possible accusations of marginalization could be politically risky. Then again, expansion of board positions could raise the overhead of the boards and slow decisionmaking.

**Importantly, growing global concerns about the adverse consequences of climate change are leading to a decline in investments in oil and gas globally, and Nigeria has not been unaffected. However, another factor explaining the decline in foreign direct investment in Nigeria’s oil and gas sector is the discovery of oil and gas in other parts of the world, including West Africa.**In fact, according to KPMG, “only 4 percent of the $70 billion investment inflows into Africa’s oil and gas industry between 2015 and 2019 [came to Nigeria](https://assets.kpmg/content/dam/kpmg/ng/pdf/tax/petroleum-industry-bill-(pib)-2020-%20a-game-changer.pdf) even though the country is the continent’s biggest producer and the largest reserves.” The declining investment in the sector is also reflected in data from Nigeria’s National Bureau of Statistics, which show that the sector accounted for 1.11 percent of aggregate capital importation into the country in 2020. **Hence, to the extent that PIA makes Nigeria competitive relative to other oil and gas producing countries,**one hoped-for benefit from the PIA is the reversal of declining investment in the oil and gas sector in Nigeria.

**Looking toward the future: Nigeria and renewable energy**

In this way, the PIA is a missed—but not lost—opportunity to position Nigeria to face a future without oil or fossil fuels. Given the “[exponential growth in renewable energy](https://www.wri.org/insights/growth-renewable-energy-sector-explained?utm_medium=social&utm_source=twitter&utm_campaign=socialmedia)” over the past 20 years, Nigeria should invest more in renewables and new energy technologies. The stipulation that 30 percent of the profit of NNPC Ltd. should be used to fund frontier basin development to include renewable energy as a frontier is a good start. The best response to competition from other African fossil fuel producers is not increasing Nigeria’s oil and gas reserves through the discovery of new reserves but increasing energy reserves. Nigeria does not need a Frontier Exploration Fund. Nigeria needs a science, technology and innovation (STI) fund, to develop new energy sources in the face of climate change and net-zero emissions targets.