

# Deep Offshore Production: 2024 Tax Incentives

**OALP** Oil and Gas Newsletter

## INTRODUCTION

As a corollary to the Oil and Gas Companies (Tax Incentives, Exemption, Remission, etc.) Order, 2024 issued by the President of the Federal Republic of Nigeria on 28 February 2024 (the **Order**), and further to the Ministers' Statutory Powers and Duties (Miscellaneous Provisions) Act<sup>1</sup>, the Minister of Finance has made public the Notice of Tax Incentives on Deep Offshore Oil and Gas Production, 2024 (the **Notice**).<sup>2</sup>

The Notice introduces a series of fiscal incentives aimed at stimulating both ongoing and future developments in deep offshore oil and gas projects. These incentives are geared towards rewarding investments in the deep offshore by offering production tax credits designed to optimize tax, ensure appreciable return on investment, and promote sustainable growth for relevant upstream players.

This newsletter highlights key provisions of the Notice and sets out the legal and regulatory considerations, as well as the broad implications of the Notice on impacted lease holders in the Nigerian petroleum industry.

## KEY HIGHLIGHTS OF THE NOTICE

### **Categories of License, & Conditions for Grant of Incentives**

The Notice introduces production tax credit incentives to two distinct categories of deep offshore developments within Oil Mining Leases (**OMLs**) and Petroleum Mining Leases (**PMLs**) that involve production sharing contracts (PSC) or profit-sharing contracts, to wit:

- Existing Leases with an approved field development plan where the lessee makes a Final Investment Decision (**FID**) between the effective date of the Notice (the **Effective Date**)<sup>2</sup> and January 1, 2029; and
- Future leases awarded after the Effective Date, including those emanating from existing and future Oil Prospecting Licences or Petroleum Prospecting Licences.

This means that current holders of OMLs and PMLs in the deep offshore that make FID between February 28, 2024, and January 1, 2029, will be entitled to production tax credit based on the volume of production.

In relation to existing leases as described above, the Notice provides for the lessee to apply to the Commission for an extension where the lessee is unable to commit to FID within the prescribed timeline on account of a Force Majeure event. Also, holders of such existing leases desirous of taking advantage of this incentive under the Notice shall notify the Commission within 30 days of making the FID.

### **Applicable Incentives for Deep Offshore Oil Development**

According to the Notice, the tax incentives are meant to incentivize investment in deep offshore development and are intended to benefit parties to the production sharing contract who have provided funding for the development.

1. Cap. M14, Laws of the Federation of Nigeria, 2004

2. The Notice is intended to take effect from 28 February 2024

3. 28 February 2024

The Notice provides for a production tax credit of:

01

the lower of **US\$3.00 per barrel or 20% of the fiscal oil price** applicable from the commencement of production up to a cumulative production of 150 million barrels where the producible reserves of the asset do not exceed 400 million barrels of crude oil equivalent; or

02

the lower of **US\$4.50 per barrel or 20% of the fiscal oil price**, applicable up to a cumulative production of 500 million barrels where the producible reserve of the asset exceeds 400 million barrels of crude oil equivalent.

03

an additional **US\$1 per barrel** in relation to future leases awarded after the effective date, from commencement of production, up to a cumulative production of 500 million barrels.

The Notice further provides that, where the crude oil price falls below US\$50, the tax incentive provided, shall apply at a reduced rate of 50% across board.

Also, where the lessee is unable to meet the requirement of having an approved field development plan, and having taken the FID, such lessee shall still be eligible for the tax credits, but at a reduced rate of 50%.

#### **Applicable Incentives for Deep Offshore Non – Associated Gas Development**

The Notice provides for a production tax credit for gas production sold from non-associated gas development, or development containing crude oil and non-associated gas in the deep offshore. The rates of the incentives are;

- the lower of **US\$1.00 per thousand standard cubic feet (mscf) of gas sold, or 30% of the fiscal gas price** of such sale, sold from the commencement of production up to a cumulative volume of 5 trillion cubic feet (TCF), where the hydrocarbon content of the field does not exceed 30 barrel per million standard cubic feet (mmscf); or
- the lower of **US\$0.5 per thousand standard cubic feet (mscf) of gas sold, or 30% of the fiscal gas price** of such sale, sold from the commencement of production up to a cumulative volume of 5 trillion cubic feet (TCF), where the hydrocarbon content of the field exceeds 30 barrels per million standard cubic feet (mmscf).

In determining the applicability of this incentive in relation to the deep offshore non-associated gas development incentives, it is important to note that; (a) the incentive does not apply where the hydrocarbon liquid content from the relevant development exceeds 100 barrels per million mscf; and (b) the determination of HCL in a non-associated gas field as contemplated shall be limited to HCL within the upstream petroleum sector and based on the guidelines of the Commission.

Also, the Notice expressly prohibits double dipping in relation to the claim of these incentives, as it provides that the applicable tax credits offered under the Notice shall not be combined with production allowance incentives provided for in the Sixth schedule to the PIA, or the Associated Gas Framework Agreement.

It is also important to note that where there is a production tax credit surplus in any year, the surplus for that year can only be carried forward for a maximum of three years.

Whilst the Notice maintains that the fiscal price for the determination of royalties shall be the same price for the calculation of the production tax credit, it is also important to note that the determination of the production tax credit shall be based on the annual total production from the development after the commencement of production and will be apportioned based on the capital contributed by each investor in the development.

The FIRS is required under the Notice to issue implementation guidelines regarding the incentives.

## SOME IMPLICATIONS FOR OPERATORS

The Notice establishes for operators under a PSC or profit-sharing arrangement in the deep offshore OMLs or PMLs, additional incentives which are aimed at attracting petroleum investment and optimizing production in the deep-offshore. We have enumerated below, essential points detailing how the Notice will affect such operators in the Nigerian oil and gas industry:

### Impact on Field Development and Investment Decisions

Given the timeline for qualified development to take full benefit of the tax credit, existing OML and PML operators will need to take a strategic decision on reaching FID in respect of some of their already approved field development plans. It is envisaged that in line with the Decade of Gas Initiative and the availability of these tax credits, there will be increased investment in Nigeria's deep offshore fields and a boost in the exploration of gas reserves especially for non-associated gas developments.

Further, by incentivizing operators to develop gas fields with lower HCL content, this may reshape exploration and production strategies within the Nigerian upstream sector, encouraging more investments in gas projects with less associated crude oil.



### Production allowance vis-s-vis production tax credit

The Notice stipulates that eligible operators would not be able to claim both production allowance and the production tax credit in any year. By implication, the Notice suggests that eligible operators can elect to either claim production allowance or the production tax credit in any tax year. This election on a yearly basis will enable such operators, after an internal analysis, to ultimately determine which of the two incentives best serve their tax optimization objective. Thus, we anticipate the FIRS' implementation guidelines to provide clarity on the modalities for claim of these incentives.



### Carry-Forward of Surplus Tax Credits

Operators are allowed to carry forward surplus tax credits of a particular year to subsequent years for a maximum of three years. This ensures that operators can optimize the use of the surplus tax credits in a particular year over a three-year period. However, where the credits remain unused beyond three years, they will expire, creating urgency for operators to use these benefits efficiently and timeously.



### Production Cost Management

To encourage cost-effective operations, the Notice introduced a cost management mechanism to encourage operators to carry out operations within a cost limit as may be determined based on regulations made by the Commission from time to time. If the sum of the unit operating cost and unit capital cost (the Unit Technical Cost) of a qualifying development exceeds the benchmark cost determined by the Commission, the tax credit will be reduced by 10%.



4. Sixth Schedule of the PIA. Production allowance for converted OMLs is the lower of \$2.5 per barrel and 20% of the fiscal oil price. For PMLs, it is the lower of \$8 per barrel and 20% of the fiscal oil price up to a cumulative maximum production of 500 million barrels from the commencement of production and the lower of \$4 per barrel and 20% of the fiscal price where production exceeds the cumulative maximum production.

## CONCLUSION

This targeted approach of fiscal incentivization could prove a prime catalyst in unlocking Nigeria's deep offshore potential thereby facilitating sustainable development of the country's petroleum resources. The Notice represents an option for PML holders to elect from production allowance under the PIA or the production tax credit under the Notice. Similarly, for OMLs, the incentives are clearly an investment enabler as there was no similar incentive in relation to NAG. It is believed that this will engender significant development in Nigeria's efforts to attract and retain investment in the gas sub-sector.

Furthermore, investment in the exploration of NAG in deep offshore assets has been encouraged with these area-specific incentives. It is however worth noting that the outcome of these incentives will rest on factors such as whether these incentives are sufficient to unlock these upstream assets to make their exploration profitable for investment. In this regard, relevant stakeholders must continue to engage to ensure that these incentives are capable of driving the intended investment.

FOR MORE INFORMATION, PLEASE CONTACT :



**Chukwuemeka Osuji**  
Partner  
[cosuji@olaniwunajayi.net](mailto:cosuji@olaniwunajayi.net)



**Olamide Obajimi**  
Partner  
[oobajimi@olaniwunajayi.net](mailto:oobajimi@olaniwunajayi.net)



**Mayowa Olusegun**  
Senior Associate  
[molusegun@olaniwunajayi.net](mailto:molusegun@olaniwunajayi.net)



**Joseph Omoba**  
Associate  
[jomoba@olaniwunajayi.net](mailto:jomoba@olaniwunajayi.net)



**Michael Cole**  
Associate  
[mcole@olaniwunajayi.net](mailto:mcole@olaniwunajayi.net)



**Jane Adekunle**  
Associate  
[jadekunle@olaniwunajayi.net](mailto:jadekunle@olaniwunajayi.net)