

Journey to Self-Sufficiency & Energy Security (Part 2): Domestic Gas Delivery Obligation

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INTRODUCTION

In Part 2 of this series, we consider the Domestic Gas Delivery Obligation (**DGDO**) of upstream lessees under the Petroleum Industry Act, 2021 (the **PIA**) and the Domestic Gas Delivery Obligation Regulations 2022 (the **DGDO Regulation**) issued by the Nigerian Upstream Petroleum Regulatory Commission (the **Commission**). The PIA and the DGDO Regulation seek to ensure that the gas demand of wholesale customers in the power sector, commercial sector and gas-based industries is met with corresponding delivery by upstream lessees. The DGDO regime is intended to ensure the efficient management of Nigeria's natural gas resources, a steady supply of natural gas for domestic use and facilitate further investments across the gas value chain. In this post, we consider the mechanism for the allocation of the DGDO under the PIA and the DGDO Regulation.

MEANING OF DGDO

The DGDO is an obligation imposed on upstream lessees producing natural gas (**Gas Producers**) to supply a certain percentage of their gas production to the domestic market. This obligation is imposed by the Commission based on the domestic gas demand requirement (**DGDR**),

which represents the total amount of marketable natural gas needed in a calendar year to supply all wholesale customers within the power sector, commercial sector, and gas-based industries (the **Strategic Sectors**).²

DETERMINATION AND ALLOCATION OF DGDO

The Commission is required to prescribe and allocate the DGDO among all Gas Producers before 1st March³ every year. Ahead of this allocation, the PIA and DGDO Regulation provide that prior to 1st February each year, upstream lessees shall provide the Commission with:

detailed information on their natural gas reserves and resources as of 31st December of the previous year;⁴

the DGDR supply curve, in \$/MMBtu and \$/Mscf, based on proved developed producing reserves⁵, proved developed non-producing reserves⁶, and proved undeveloped reserves⁷; and

existing and additional gas purchase orders and sales agreements.

1. Wholesale Customers are the class of customers designated with the right to contract for and purchase a supply of wholesale gas, with a capability to connect individually and economically to a transportation pipeline or transportation network and shall include gas distributors.
2. Section 173 of the PIA.
3. Section 110 of the PIA.
4. Regulation 3 of the DGDO Regulation.
5. These are proved developed reserves which are expected to be recovered from completion intervals, which are open and producing at the time of the estimate.
6. These are proved developed reserves which include shut-in and behind pipe reserves.
7. These are Proved reserves expected to be recovered from (a) new wells on undrilled acreage, (b) deepening existing wells to access different reservoirs, or (c) significant investments to recomplete wells or install production/transportation facilities for improved recovery.



Upon receipt of the information by the Commission, the Commission will create a comprehensive national supply curve, the “national domestic gas demand requirement supply” (NGDRS) curve. The NGDRS curve is the supply curve of natural gas to be supplied on a voluntary basis for a specific price level by the Gas Producers, and this forms the basis for the allocation of DGDO to Gas Producers.⁸

VOLUNTARY ARRANGEMENT FOR FULFILMENT OF DGDO

Gas Producers may voluntarily execute contracts with wholesale customers of Strategic Sectors or execute contracts with wholesale gas suppliers supplying the Strategic Sectors.

Once executed, the Gas Producer is obliged to notify the Commission and the Nigerian Midstream and Downstream Petroleum Regulatory Authority (NMDPRA)⁹. To the extent that the volumes to be sold under the contract(s) satisfy or exceed the DGDO, the Gas Producer shall inform the gas aggregator¹⁰, and shall be excluded from the mandatory regime for fulfilment of the DGDO.

MANDATORY ARRANGEMENT FOR FULFILMENT OF DGDO

In the event a Gas Producer is unable to execute a gas supply agreement directly with a wholesale customer or wholesale gas suppliers supplying the Strategic Sectors, the affected Gas Producer shall have an obligation to deliver such volumes of gas to any wholesale customer determined by the gas aggregator pursuant to a gas purchase order issued by the gas aggregator.¹¹

SATISFACTION OF DGDO, A CONDITION FOR EXPORT AND SALE TO OTHER SECTORS

A Gas Producer shall only be permitted to supply natural gas to: (i) wholesale customers in non-Strategic Sectors; or (ii) new midstream gas export operations, after it has met its DGDO.¹²

DETERMINATION OF DOMESTIC GAS SUPPLY PRICE

While section 167 of the PIA assigns the NMDPRA with the responsibility for determining the domestic base price for gas sold to the Strategic Sector, the Commission plays a key role in the process for determination of the domestic base price by determining the domestic gas supply price.

The Commission is obliged to identify on the NGDRS curve the lowest¹³ price for which the total DGDR for the Strategic Sectors shall be supplied, considering the production profiles of the proved developed producing reserves and timelines for execution of any proposed projects to increase gas production. This price is the “domestic gas supply price”. The price is then forwarded to the NMDPRA before March 15 each year, and is used as a benchmark for determination of the domestic base price.¹⁴

ENCOURAGING WORKS AND INVESTMENTS TO SATISFY DGDO

Depending on the DGDR, state of existing gas infrastructure and status of a Gas Producer’s gas reserves, the Commission may direct Gas Producers to carry out certain works and operations such as (re)completion of a well, drilling new wells, deepening existing wells, construction of gas transportation pipelines, and investment in renewable energy.¹⁵

Furthermore, the Commission, in consultation with the Midstream and Downstream Gas Infrastructure Fund, may encourage a Gas Producer to invest in the construction of additional gas infrastructure if there is no spare capacity in existing gas infrastructure.¹⁶

8. Regulation 4(1) and (2) of the DGDO Regulation.

9. Section 110(3) of the PIA

10. In Nigeria, the gas aggregator is the Gas Aggregation Company Nigeria.

11. Section 110(7) and 156 of the PIA.

12. Section 110 (14) of the PIA

13. Paragraph 2(a)(ii) of the Third Schedule of the PIA provides that in establishing

the criteria for the allocation of domestic gas delivery obligations, the pricing of gas for the domestic market shall be based on the lowest cost of supply of gas available in the three-tier classification of supply sources for the domestic market.

14. Regulation 5(2) of the DGDO Regulation.

15. Regulation 7(1)-(6) of the DGDO Regulation.

16. Regulation 7(5) of the DGDO Regulation.

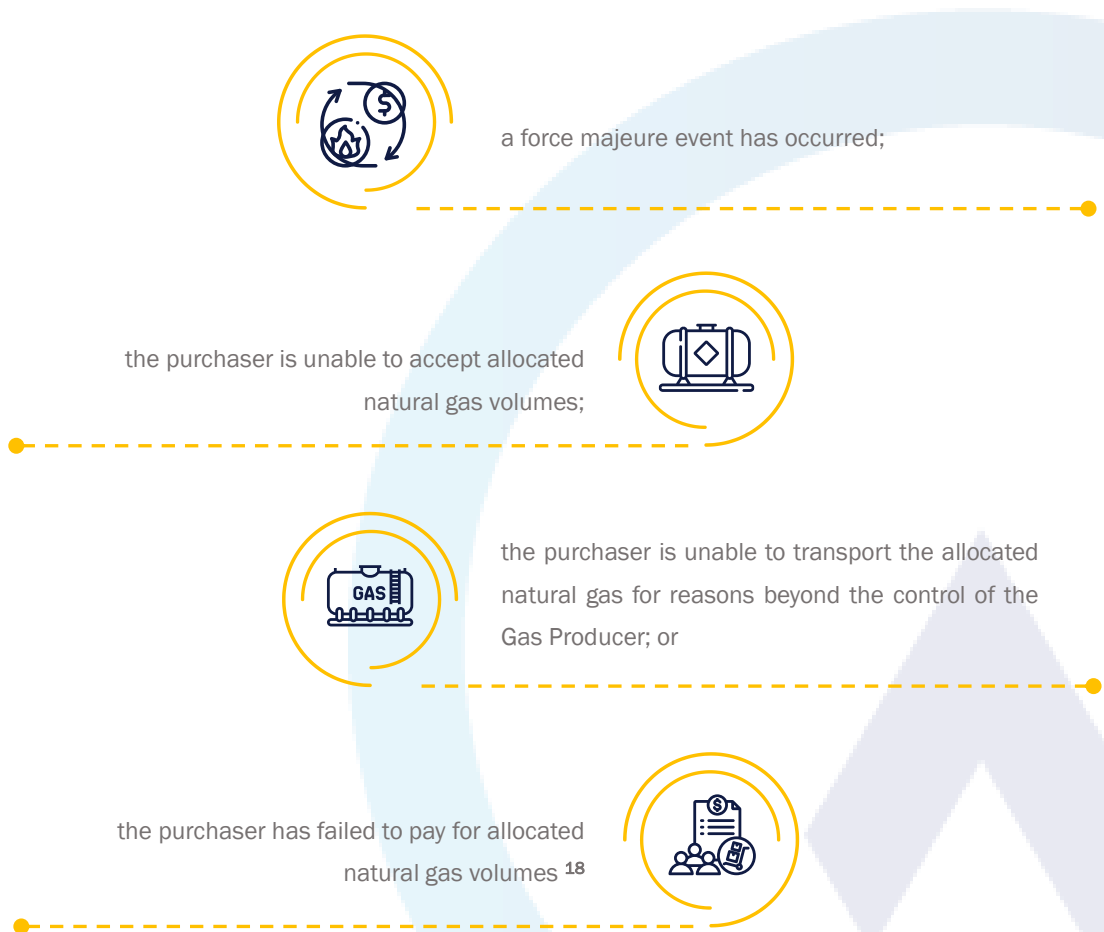
PHASING OUT DGDO IN NIGERIA

By the provisions of the PIA, the imposition of DGDO will only be discontinued after the NMDPRA has determined that the natural gas market has attained full market status.¹⁷

PENALTY FOR FAILURE TO MEET DGDO

As a deterrent, the PIA imposes a pecuniary penalty to the tune of US\$3.50 per MMBtu for gas not delivered by a Gas Producer pursuant to the allocated DGDO. The penalty serves as the minimum threshold, even if otherwise has been agreed in any gas sale agreement with a wholesale supplier or wholesale customer.

However, a Gas Producer would be exempt from imposition of this penalty if the failure to deliver is because:



17. Section 110(11) of the PIA.

18. Section 110 (8)-(10) of the PIA, Regulation 6 of the DGDO Regulation.

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