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CASE STUDY OF AN INSOLVENT OIL AND GAS ASSET HOLDER IN THE NIGERIAN PETROLEUM INDUSTRY: MATTERS ARISING [PART 3]

INTRODUCTION

The 2 recent cases which highlight the issues arising in the transfer, assignment and acquisition of interests in oil and gas assets in Nigeria induced by insolvency are the cases of Afren Petroleum Plc (“Afren Plc”) and Allied Energy Limited - Holder of OMLs 120 & 121 (“Allied Energy”). We provide at the outset, a highlight of the facts and decisions of the said cases and commentary with illustration of the matters arising from them.

Afren Plc was listed on the London Stock Exchange and it went bust in a spectacular manner a few years back, with repercussions for various Nigerian oil and gas assets. The delay in sanctioning the transfer of Afren Plc’s interests in Nigerian oil and gas assets has raised a lot of concerns for investors, stakeholders and the regulator - the Department of Petroleum Resources (“DPR”). The decision in the Afren case was handed down by the Federal High Court in **LEKOIL 310 Limited and Afren Investment Oil & Gas (Nig.) Ltd. v. Minister of Petroleum Resources and Optimum Petroleum Development Company Ltd** and this case typifies the issues discussed in this paper.

(i) Background of the case

- Afren Plc is the parent company of two Nigerian companies holding interests in several assets. In particular Afren Nigeria Limited (“ANL”) holds a 40% participating interest in OPL 310, which is operated by Optimum Petroleum Limited.

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- ANL transferred 17.14% of its participating interest in OPL 310 to Mayfair Assets and Trusts Nigeria Limited, a subsidiary of Lekoil Limited, in February 2013 with the consent of Optimum Petroleum Limited.
- Lekoil applied for the Minister's approval of its acquisition of this 17.14% participating interest in 2013 but only received approval in June 2017.
- Afren Plc entered into administration in 2015 and the administrator agreed to sell the remainder of ANL's participating interest in OPL 310 to Lekoil Limited in the name of a third company called Lekoil 310 Limited ("Lekoil 310").
- Lekoil assumed ownership of the remaining 22.86% interest it acquired from the administrator of Afren Plc without the consent of Optimum Petroleum Limited, but subject to the approval of the Minister. Lekoil applied for the consent of the Minister in 2016 but this was neither granted nor rejected.
- The Plaintiffs, Lekoil 310 and Afren Nigeria Oil & Gas Investment Limited took out an originating summons against the Defendants, praying the Court to deem as validly granted, Lekoil 310's acquisition of the additional 22.86% participating interest in OPL 310.

(ii) Arguments of parties

The Plaintiffs admitted that the Guidelines and Procedures for Obtaining Minister's Consent to the Assignment of Interest in Oil and Gas Assets ("the Guidelines") made the Minister's consent a condition-precedent for a valid transfer of oil and gas assets. They however, contended that by section 3 of the **Executive Order for the Ease of Doing Business of May 2017** ("the Executive Order"), the 1st Plaintiff's application for the consent of the Minister was entitled to a "default approval" since the Minister failed or neglected to communicate approval or rejection of the application.

Conversely, the Defendants responded by stating that the Executive Order cannot be made to have retroactive effect as it was made in 2017, two (2) years after the application for the consent of the Minister was made. The Defendants further argued that the application for Minister's consent made in 2015 was incomplete and therefore invalid.

(iii) The Court's decision

The Federal High Court dismissed the suit and held as follows:

1. That the consent of the Minister is a fundamental requirement for the validity of any assignment or transfer of interest in oil and gas assets;

2. That the consent as aforesaid cannot be granted by “default”. The consent of the Minister must be “**positive, affirmative and definite**”;
3. That the acquisition of share capital and resulting participating interests of the 2nd Plaintiff over OPL 310 by 1st Plaintiff is “inchoate and invalid”; and
4. That the provisions of Executive Order of May 2017 for Ease of Doing Business are inapplicable to the instant application for Minister’s Consent.

(iv) Observation on the judgment.

The Nigerian Federal High Court was not persuaded that the consent of the Minister could be deemed as granted in any circumstance. The court applied the literal interpretation to the statutory provisions of the Petroleum Act and the applicable regulation and guidelines, but not the Executive Order. It seems the Executive Order would not have been allowed to apply to change the statute and applicable regulation and guidelines in respect of consent of the Minister even if the application for consent had been submitted after the Executive Order was made, and not before as in this case. Consent of Minister is required in all circumstances of change of ownership.²

Allied Energy: The critical points to note in this complex multijurisdictional case are as follows:

- Nigerian Agip Exploration Limited (“NAE”) had 40% equity interest in both OMLs 120 and 121.
- In 2012 NAE sold its interest to Allied Energy Limited (“Allied”) for about USD 200 Million which Allied failed to pay. NAE won an arbitral award against Allied (and its affiliates and parent companies) and enforced the Award through a court order, which led to the locking of the OYO field export valve. Prior to the locking of the export valve it was established that there was about 380,000 barrels of crude oil on the FPSO awaiting export.
- Prior to the above Erin Energy Corporation (“EEC”) a publicly quoted company which ultimately filed for bankruptcy in the United States had acquired Allied and its interests in the OMLs without the consent of the Minister.
- EEC’s bankruptcy effectively ended Allied’s operations. Production on the OMLs ceased and the company has been unable to meet its obligations to its service providers, creditors, personnel and most importantly the Federal Government of

² First Schedule, Paragraph 14, Petroleum Act and Regulation 4 of the Petroleum (Drilling and Production) Regulations (the Regulations). See also *Moni Pulo Limited v. Brass Exploration* FHC/L/CS/835/11.

- Nigeria to whom it owes substantial royalties and gas flare fees in the sum of about USD36m.
- Allied's major creditors, Zenith Bank Plc, Bumi Armada (Singapore) Pts Ltd (BASPL) and Public Investment Corporation (PIC) South Africa obtained a court judgment in Nigeria staying all foreign proceedings against all assets of EEC (including Allied) and ultimately appointing a receiver manager for the purposes of disposing of the crude on the FPSO.

Observation on the judgment: This case threw up issues around the rights and duties of a receiver manager/administrator over the assets of an insolvent oil and gas licensee or lessee as well as questions as to what constitutes oil and gas assets in the event of an insolvency. There is a question as to whether the 380,000 barrels of crude oil on the FPSO awaiting export constitutes an oil and gas asset of the licensee or lessee? There is also a question as to whether a receiver/receiver manager appointed by a creditor can take over and operate an oil and gas asset and exercise powers and rights prior to or without the Minister's consent in Nigeria?

Summary of the various Problems in Relation to Insolvency in the Oil and Gas industry

The problems thrown up by the insolvency proceedings in the oil and gas industry i.e. to the insolvent license holder, the creditor, the receiver or receiver manager, the Minister of Petroleum Resources, and the DPR among others, can be summarized as follows with respect to the challenges they present the DPR, and with the following points/questions in view:

- The DPR does not have full knowledge of the facts and circumstances surrounding most of these insolvencies as the underlying finance agreements are generally not registered with or made available to the DPR;
- These insolvencies raise implications on the continued operations of the affected oil and gas assets in Nigeria, and the rights of administrators/receiver managers appointed by the creditor to deal with or manage such assets;
- In the case of an application by the administrator/receiver manager for consent to transfer the interest in the Nigerian assets, it is not clear what the proper treatment of such applications by the DPR will be in view of contending interests by other interested parties - the Federal Government, interest holders, creditors, contractors, and employees;

- Even though, an oil and gas lease or license can only be issued to a Nigerian registered company³ in case of foreign insolvencies, DPR may encounter difficulties in obtaining full and timely information as to the incidence of insolvency as the Minister or DPR may not likely be a party to the foreign proceedings until the result is brought back home for enforcement;
- Many license holders source their funds using their foreign entities, foreign parent company or shareholder with a direct or indirect interest in the licensee or leaseholder, thus compounding the structural complications.
- The additional complications or dynamics that may arise with cross-border insolvencies is that the DPR may not have a full grasp of the facts and circumstances surrounding the insolvency so as to deal with the consequences effectively and minimize the downtime in the operation of the field/asset.
- In a case where it is the insolvency law regime of another jurisdiction that produces the receiver/manager or administrator appointed, this can create additional complexity for the DPR and have implications for the power to control or regulate the activities of the receiver/manager or administrator as insolvency regimes of countries differ one from another.
- Insolvency proceedings involving the holder of an oil and gas asset impacts the interests of the asset holder directly as the creditor will seek to take over the asset, and it becomes the role of the asset-holder insolvent company to obtain the consent of the Minister to that acquisition, take over or assignment. This scenario presupposes that the insolvency is a non-contentious one. Even then, the insolvent asset holder may not be able to secure the consent of the Minister in a timely manner or at all. This is what happened in the Afren case considered earlier.
- Another possibility is that the insolvency may give rise to contentions between the asset holder and its creditor(s), which, if not resolved on time, will render the asset holder incapable of complying with the conditions of the licence or lease.
- In either case, the creditor, who is seeking to take over the asset or a third party to whom the asset is to be transferred are unlikely to commit more funds to the project as their interest is not secured without the Minister's consent.
- The project may thus become inoperative or not be properly funded and production may shut down. Demobilization of security, personnel and other associated services

³ Section 2(2) of the Petroleum Act provides that "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".

on the asset are signs of such problems and can be signs of insolvency. This is what happened in the case of Allied Energy Limited earlier reviewed.

- An insolvent oil and gas company will persistently refuse to remit or often withhold deducted taxes, and royalties to the appropriate tax and governmental authorities. Such company will also find it impossible to have access to cash to meet its immediate financial obligations and the conditions of grant of the licence or lease will be adversely affected.
- It must be noted that there is no clear provision of the law barring the receiver/administrator of an insolvent licensee or lessee from dealing with the assets of an oil and gas company under Nigerian law. In dealing with an oil and gas asset however, the receiver/administrator must exercise its powers in accordance with the Petroleum Act and may not further assign an asset prior to obtaining the consent of the Minister.⁴
- When an interest holder becomes insolvent, the Minister of Petroleum Resources generally does not have the power to terminate the licence or lease on that ground alone except where the insolvency has led to a breach of any of the terms and conditions of the licence or lease or any of the provisions of the Petroleum Act.
- Where signs of insolvency are shown in respect of an asset, the Minister of Petroleum Resources, through the DPR can flag the distress and request the asset holder to remedy the identified issues in suggested way(s) or in line with the terms and conditions of the licence or lease.
- The Minister's power to revoke a licence or lease is not a power that is usually exercised lightly, particularly where insolvency is the underlying cause of the inability of the licensee or lessee to fulfill its obligations Government would be mindful of the fact that exercising the power to revoke a lease or licence for non-compliance arising from insolvency will have an impact not only on the licensee or lessee but also on their creditors. In such circumstance, a revocation will effectively truncate the ability of the licensee or lessee's creditors to recoup their exposure from the asset that formed the security for their lending. This would send a wrong signal to the industry and make financing difficult to obtain. These considerations are aptly captured in the provisions of **paragraphs 26, 27 and 28 of the First Schedule to the Petroleum Act** which require the minister to communicate grounds of any proposed revocation

⁴ See Section 17(5)(d) of the Oil Pipelines Act 2004 and Para. 14 of the First Schedule to the Petroleum Act 2004.

to the asset holder and give it adequate opportunity to give explanations and rectify the default before ordering a revocation.

- Also, it would seem that the Joint Operating Agreements (“JOAs”) of existing companies do not adequately address insolvency, to facilitate commercial resolution of insolvency matters or that the JV partners often do not comply willingly with their terms and agreements.

In concluding this part, it is obvious from the above that there is sizable quantum of issues which the stakeholders, and particularly the regulator and government have to deal with in the industry. In the next part of this paper, which has the title “**The Powers of the Minister of Petroleum Resources where an Oil and Gas Asset or Interest Holder becomes Insolvent**” we will examine the current powers of the Minister of Petroleum vis-à-vis other stakeholders’ powers in dealing with an insolvent oil and gas asset or interest holder. Can the Minister simply revoke the title or does he or she need to wait until certain threshold of default in the terms and condition of the licence is observed? Even when the decision to revoke is made, what steps must the Minister take in addressing the problem.

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