AN ANALYSIS OF THE EFFICACY OF FISCAL LAWS RELATING TO PETROLEUM OPERATIONS IN NIGERIA

BY

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REG. NO.: LAW/LLM/16518/2007-08

A THESIS SUBMITTED TO THE POSTGRADUATE SCHOOL OF AHMADU BELLO UNIVERSITY, ZARIA, NIGERIA
IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF LAWS - LL.M.

DEPARTMENT OF COMMERCIAL LAW
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JUNE 2011

DECLARATION

I, ASHANG TANKO, hereby declare that this THESIS has been written by me and that it is a record of my own research work. No part of this THESIS has been presented or published anywhere, at anytime, by anybody, institution or organisation or for the award of any academic degree.

ASHANG TANKO

CERTIFICATION

THIS THESIS, entitled **AN APPRAISAL OF THE EFFICACY OF FISCAL LAWS RELATING TO PETROLEUM OPERATIONS IN NIGERIA**, by **ASHANG TANKO** meets the regulations governing the award of Master of Laws (LL.M.) of the Ahmadu Bello University Zaria, Nigeria and is approved for its contribution to knowledge and literary presentation.

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DEDICATION

This THESIS is affectionately DEDICATED

To my wife,

BRIDGET,

Whose integrity and determination to surmount difficulties have been a constant invigorating inspiration.

ACKNOWLEDGEMENT

Many persons and institutions have contributed immensely to making the writing of this thesis a reality. It is an impossible task to list them all. However, I just have to mention a few such persons and institutions. First I thank God the Father, the Son and the Holy Spirit for guidance, inspiration, grace and wisdom to undertake this programme and complete this work. Followed at a respectful distance is the guidance and contribution as well as the support from my supervisors, the ever reliable and amiable DR A.A. AKUME and DR D.C. JOHN. I thank the Nigerian tax Authority - the Federal Inland Revenue Service - which offered me the opportunity to appreciate taxation and develop an interest in further studies on the subject. It is an institution of integrity, excellence and transparency. I am greatly indebted to the Executive Chairman of the Service, Mrs. Ifueko Omoigui-Okauru who gave me access to firsthand information and built my confidence in the subject, not to mention her constant encouragement to excel.

My sincere gratitude goes also to Mr Friday Onamson, who worked with me in the manner of a twin brother all through my studies and writing of this thesis. I thank Mrs Laah and Alhaji Maye and other staff of ABU, particularly those of the Library for their consistent cooperation. I acknowledge the enormous assistance rendered me by my warm, friendly and able supervisors whose reviews and comments greatly enriched my work.

I register special gratitude to the National Emergency Management Agency and its management staff, especially the former Director-General of the Agency, AVM M.M. Audu-Bida (Rtd), and the current Director-General, Alhaji Muhammad Sani Sidi, for his patience, moral and material support and his understanding throughout my studies and while writing this thesis. I thank my friend and colleague Alhassan Esq for constantly being at my side and travelling with me on this exercise. I am grateful to my former staff Suleiman Lawsl Esq, who ran errands for me while this exercise lasted. I thank my young friends Mary Gali, Anita Egwuonu Esq and Taiye

Apologun (my ever hardworking Secretary) for their encouraging work towards the success of this thesis. I thank especially Tina Atala Esq, my friend and confidant, for her critical reviews and dedication to this work. And last but by no means least, I would like to pay special tribute to the patience and understanding of my family and friends, who have had to endure my preoccupation with this thesis for the best part of two years.

ABSTRACT

Petroleum has become the number one resource in the world because of its universality. All other resources are demanded in varying scales, but not petroleum. However the catch is that while demand increases, existing production of this pearl declines. In Nigeria, the problem appears to be a double-edged sword. Declining production and the apparently doubted efficacy, and confused state, of the fiscal laws relating to petroleum operations in the country remain intractable problems which the government is grappling with. This calls for a re-examination of fiscal policy.

Thus taxation is an inherent element of fiscal policy. The petroleum industry as a major revenue earner for the government is not immune from this inherent element. However, concerns surround the efficacy of the fiscal law relating to petroleum operations having regard to the hackneyed calls for, and untiring efforts at discovering, cheaper alternative sources of energy, in a world whose economic activities are now unleashing backlash effects in the form of ozone layer depletion, global warming and other environmental concerns. More than this fear however, the government itself recognises that something is wrong somewhere regarding the beneficial effects or rewards of petroleum to the Nigerian people, having decried the porosity of the fiscal regime relative to the petroleum sector.

Yet the fiscal regime of petroleum operations in Nigeria appear to be 'very strong' when viewed against the backdrop of plethora of legislations specific to this area. The PPTA, the CITA, the PSC Act and the Incentives Act, apart from other related legislations which have elements of fiscal policy, are principal legislations here. Natural with man to find walk around for impediments, it would appear that some of these legislations are hewn in such a way that it amounted to emasculating the Nigerian economy, sabotaging the rights of the Nigerian people to development and impeding economic independence of the nation, so that, on account of the latter, the economic structure of the country is perpetually neo-colonialist. Aware of these dangers, the government embarked on a reform agenda of petroleum operations in Nigeria, propped by the well conceived Petroleum Industry Bill (PIB) 2008.

With the passage of the FIRS (Establishment) Act 2007, the stage appears set for marked improvement in the revenue to be generated from this prime economic

resource. The Act and the PIB 2008 (if eventually passed into law) will undoubtedly concatenate to deliver a measure of transparency, responsibility and accountability with respect to fiscal regime governing this sector. But this is as far as administrative and legal framework is concerned. Sadly, in a desperate bid to save the system, the government adopts carrot-and-stick measures. In the alternative, what is needed, among others, is a responsible political system where infrastructural facilities are not epileptic or waning, where energy supply (in terms of power) is steady and stable, where security of lives and property is not a daydreaming fantasy and where good governance framework is the avowed commitment of the government. These are the key elements of realising and sustaining the efficacy of the fiscal regime attending to petroleum operations in Nigeria.

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CHAPTER ONE

GENERAL INTRODUCTION

1.0 INTRODUCTION

FISCAL as a word has two etymologies,[1] and it relates to taxation, public revenues or public debt management and policies.[2] Normally, we speak of fiscal policy, which is a deliberate governmental action that attempts consciously to control the actions of individuals and companies by means of spending and taxation decisions. It has been stated that the expenditure side of fiscal policy could be achieved by spending money in ways that stimulate other activity.[3] Whereas fiscal policy as it relates to taxation can affect work, investment or production decisions by changing tax rates and levels.

Thus, fiscal policy effectually strikes a balance between the resources the government puts into the economy through expenditures and that it takes out through taxation, charges or borrowing. When government takes the bold step of concretising its fiscal policy the end product is laws, for instance tax laws, or policy statements, for instance budgets. For our purposes, we are concerned with the fiscal policy as it relates to what the government takes out through taxation. In other words, any reference to fiscal laws in this work means those laws that touch upon taxation, and more specifically the taxation of petroleum operations in Nigeria.

Taxation plays a central role in matters of fiscal policy. This role was emphasized by the United States Supreme Court when **Justice Potter Stewart**[4] made an astute observation regarding the pervasive nature of taxation. According to the Learned Justice,

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[1] In French, it is called *fiscus*; In Latin it is called *fiscalis.*
[2] Webster's Third New International Dictionary (Unabridged), Massachusetts: Merriam-Webster, 1993, p. 857.
[3] **"fiscal policy."** Encyclopædia Britannica. Ultimate Reference Suite. Chicago: Encyclopædia Britannica, 2010.
[4] **United States v. Bisceglia** (1975) 420 U.S. 141, 154

"virtually all persons or objects in this country… may have tax problems. Every day the economy generates thousands of sales, loans, gifts, purchases, leases, wills and the like, which suggest the possibility of tax problems for somebody. Our economy is "tax relevant" in almost every detail".

No wonder, then, that the petroleum sector of the Nigerian economy is not immune from the pervasive tendencies of taxation, an inherent element of fiscal policy. However the reason for this is not farfetched: the petroleum industry is a major revenue earner for the government, through, among others, royalties, bonuses, rents, percentages from the production sharings contract, taxes, etc.[5]

Principally, the Nigerian petroleum industry is divided into two broad categories: upstream operations and downstream operations. There is an adjunct to the petroleum industry, natural gas operations. Upstream operations involve exploration and production of crude oil, under governmental grant of licence[6] by companies for sale or disposal. On the other hand, downstream operations involve those activities which culminate in value addition and improvement upon the end product of upstream operations. In other words those companies engaged in refining and distribution of petroleum products are captured here. Natural gas is a colourless, highly flammable gaseous hydrocarbon consisting primarily of methane and ethane and it is a type of petroleum that commonly occurs in association with crude oil. Thus both natural gas and crude oil are hydrocarbons. In this work natural gas is classified under petroleum operations, though as an adjunct and will be so treated.

[5]Omorogbe, Y., **Oil and Gas Law in Nigeria**, Lagos: Malthouse Press Ltd, 2001, p. 65.
[6] Under the Petroleum Act CAP. 350 L.F.N. 1990; ACT CAP. P10 L.F.N. 2004, there are three types of licences granted by the government, namely ***oil prospecting licence, oil mining licence and oil exploration licence.***

Significantly, different regimes of fiscal laws relate the various outlined sectors of the Nigerian petroleum industry.[7] For instance, the **Petroleum Profits Tax Act CAP. 354 L.F.N. 1990; CAP. P13 L.F.N. 2004** (as amended) relates to upstream operations; the **Companies Income Tax Act CAP. C21 L.F.N. 2004 (AMENDED BY COMPANIES INCOME TAX (AMENDMENT) ACT NO. 11 2007)** applies to downstream operations; and the **Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Decree No. 39 of 1990**. This latter Decree was amended by **Nigeria LNG (Fiscal Incentives Guarantees and Assurance Decree 113 of 1993, now CAP N87 LFN 2004**. It is intended therefore to undertake an analysis of the above laws in order to discover whether or not they are efficacious by bringing about the naturally and reasonably intended results for their enactment, to wit enhanced revenue base of the government of Nigeria.

The above point leads to confirm the "interest factor" which underpinned, motivated and inspired the researcher in this area to undertake an analysis of the efficacy of such laws. Laws do not exist in a vacuum but exist within a socioeconomic context, in this case the context of petroleum operations. Thus, despite the existence of fiscal laws, for instance relating to upstream petroleum operations in Nigeria, the government has had to take certain steps which unwittingly are meant to "help" the law – for example, the regime of production sharing contracts, which significantly varied PPTA tax rates from 85% to 50%. Does it mean that the fiscal law is a disincentive to investment, and thus revenue in this area of petroleum operations in Nigeria? There is the myriad of incentives granted, under a statute, to the Nigeria LNG. One of the guarantees which the government of Nigeria undertook is that "the Nigeria LNG and its shareholders shall not be subject to new laws, regulations, taxes,

[7] These laws and others will be explored in greater detail under their appropriate Chapters and headings.

etc, which are not generally applicable to companies incorporated in Nigeria".[8] In other words different tax regimes cannot be made to apply to it, like for instance, the case of other upstream operators. Now that the world market price of crude continues to take a downward spiral, is it not time that a second look was taken at this law? These are some of the burning issues which informed the choice of this area of the research.

1.1 STATEMENT OF THE PROBLEM

Apart from being one of the largest economies in Africa, the Nigerian economy has since the late 1960s been based significantly, and almost entirely, on the petroleum industry. This attitude of the Nigerian government, overtime, showed up its dysfunctional consequences on the economy. In fact, this caused agricultural production to stagnate to such an extent that cash crops like palm oil, peanuts (groundnuts), and cotton were no longer significant export commodities while Nigeria was forced, till date, to import such basic commodities as rice for domestic consumption. This untoward system worked well as long as revenues from petroleum remained constant. This is one of the serious problems that this research sets out to address.

Today, the story is no longer the same, because there has been unabated fluctuation in world oil market prices, with incessant call for concerted efforts for alternatives to petroleum. Market fluctuation, whether upwards or downwards, does not augur well for fiscal policy, because it tends to distort

[8] Omorogbe Y., Oil and Gas Law in Nigeria, Mathouse Press Limited, 2001, p. 76.

governmental programmes. Sadly, the frequency of market fluctuation is normally not directly correlated to fiscal law in place. That is, when market price fluctuates that impinge upon governmental plan, the law does not change *mutatis mutandis* to reflect the new market direction and thus shield government revenue from such changes. Secondly, there has been increasing call for less dependence on oil by developed economies of the world, the main market for our oil exports. Leading in this call and search for alternative source of energy is the world's largest economy, the United States with the present administration of President Obama appointing a Harvard Scientist to lead the way in this search. If the above picture becomes true to type, then the revenue available to the Nigerian government will, without doubt, plummet with its adverse effects upon an already dysfunctional economy. Thus, this research will address the problem which this will throw up and how the fiscal laws relating to petroleum will be proactively directed at mitigating the impact of this imminent paradigm shift of global proportions.

Further and related to the above problem is important questions thrown up and sought to be addressed by this Research:

1. That is, in the face of plummeting revenue from petroleum operations, what role does, or will, the fiscal laws thereto play to shield the government from its adverse repercussive effects?

2. The above question will lead yet to another problem, whether the fiscal laws as presently constituted, existing and operational with respect to petroleum operations in Nigeria are potent enough to ensure that the government generates sufficient revenue and thereby build formidable foreign

reserve which will enable the government to develop its untapped and neglected agricultural potentials, its manufacturing sector, and its infrastructural framework in order to build an economy, nay a society where her people will have comparable and meaningful standard of living. In other words, what is the extent of the efficacy of the fiscal laws relating petroleum operations in Nigeria, as it relates to revenue/financial security of Nigeria and her people?

1.2 OBJECTIVE OF THE RESEARCH

All hands must be on deck to avert the imminent danger posed to the revenue of the Nigerian government, by dwindling resources from petroleum operations. This danger will probably be exacerbated by the future prospect of a more efficient source of energy. In other words, as a people we must evolve a creative, workable and effective ways of overcoming the problem. Thus this Research came out with a proposal (or recommendation) for workable fiscal mechanisms which will enable the government whittle down the likely consequences on the Nigerian economy that will ensue from revenue crisis due to marked drop in world market for crude oil.

To attain the above overall objective, this Research identified and analysed the fiscal laws pertaining to petroleum operations in Nigeria, which involve upstream, downstream and natural gas operations. Thereafter, an attempt was made to establish a nexus between the fiscal laws and the revenue derivable from petroleum operations in Nigeria. To do this, the Research distiled and articulated operational and implementation issues, with respect to

the fiscal laws. It is hoped that an analytical consideration of these issues will dovetail into the overall objective.

1.3 SCOPE OF THE RESEARCH

This research was not intended to be open-ended, and thus it is not anticipated that the scope of the research will extend to cover all aspects of the subject. Thus, the research focussed on the analysis of the efficacy of the fiscal laws relating to petroleum operations in Nigeria. These include:

(a) The **Petroleum Profits Tax Act CAP. 354 L.F.N. 1990; CAP. P13 L.F.N. 2004** (as amended) that relates to upstream operations;

(b) Part VIII – Fiscal Provisions of the Petroleum Industry Bill, 2008

(c) The **Companies Income Tax Act CAP. C21 L.F.N. 2004 (AMENDED BY COMPANIES INCOME TAX (AMENDMENT) ACT NO. 11 2007)** that applies to downstream operations; and

(d) The **Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Decree No. 39 of 1990**, as amended by **Nigeria LNG (Fiscal Incentives Guarantees and Assurance Decree 113 of 1993, now CAP N87 LFN 2004**, that is applicable to natural gas operations.

The scope of this research does not include coverage of other tax laws in Nigeria. It was not intended also to veer into double taxation agreements, tax planning, etc. As much as relevant to the research certain specific tax offences will be covered.

1.4 METHODOLOGY

The methodology to be used in this research is doctrinal: the statutes dealing on fiscal laws relating to petroleum operations, in line with the scope of the research, as a primary source, have been consulted, analysed and inferences drawn there from. The secondary sources are textbooks, journals publications, and internet resources.

1.5 JUSTIFICATION

The topical significance, and thus justification of this research needs not be overemphasised. First and foremost, it will be an instrument for sound fiscal policy. Fiscal policy helps the government to achieve its allocative efficiency through proper tax system. Since the research focussed on analysing the efficacy of fiscal laws relating to petroleum operations in Nigeria, it is hoped that the results of this research would in no small measure enhance government's revenue by identifying the strengths and weaknesses of the laws as presently constituted and proffering remedial actions. This research would also benefit practitioners, lawyers and accountants, and students. For practitioners it would be an easily available and current reference manual for their practice of taxation as it relates to petroleum operations in Nigeria. For students, it will open up their understanding and regenerate their interest in the technical field of petroleum taxation, which, it is hoped, will ultimately lead to increased research in this area.

1.6 LITERATURE REVIEW

In the course of this research, the writer intended to consult widely several literatures where relevant contributions have been made to the area of the research. As much as possible, law reports, academic journals and applicable statutes will be profusely consulted. The views of the writers will be critically

analysed in the light of statutory provisions, with a view to coming up with a fresher insight based on current and present developments,

Thus, despite the recent of the works of **Etikerentse**[9] and **Arogundade**[10], they appear to have been overtaken by present developments, to wit the FIRS Act 2007 and CITA 2007, with the effect that the positions taken by the authors in some areas are, today, not the law, or have been modified by the present state of the law. For example, despite the submission of Arogundade at page 311 that "self assessment programme in Nigeria has proved to be a very ineffective tax measure", because "it is embraced only by the big companies that stand to gain from the 1% filing bonus and the instalment payment concessions it confers", the **Companies Income Tax (Amendment) Act 2007** made self assessment compulsory by all companies. In fact to show the apparent success of the programme against the submission of the author, the Amendment law removed the one percent filing bonus, and created a late filing penalty of N25,000.00 after 30th June and N5,000.00 for every subsequent month in which the default of late filing persists. In other words, it may not be totally true that the programme is a failure, however it has a tendency to increase nonchalance and complacence towards field based tax audit.

Further, the **Federal Inland Revenue Service Act 2007** is another enactment which revolutionised the taxing situation of petroleum operations companies in Nigeria. Thus, it is clothed with new and novel powers in aid of its administration and enforcement powers. This is not surprising, because the strength of any law lies in its administration and enforcement. Thus, for the

[9] Nigerian Petroleum Law, 2004.
[10] Nigerian Income Tax & Its International Dimension, 2005

first time, the FIRS is given power to request from any bank information regarding any petroleum operations company in Nigeria, and the bank is, under pain of fine of not less than N500,000, duty bound to comply. However, the quantum of fine can be said to be paltry, when the extent of the operations of the petroleum companies are considered. This means that such companies could encourage their bankers to disregard the request of the FIRS.

In addition, the FIRS has powers to investigate any person whose standard of living does not correlate with the extent of his income. This provision is targeted at ostentatious and extravagant lifestyle of senior executives of companies, who milk their companies, while under-declaring their turnover in order to pay less tax. This is supplemented by another provision which this writer calls whistleblower provision. This provision aimed at encouraging community participation in procuring compliance to tax payment by companies. Thus, any person who gives useful and relevant information to the FIRS shall be paid compensation, determined and approved by the Board. However, the process of giving the compensation can be a bottleneck to this provision, so that it may be good in the books than in practice.

Comprehensively, there is the **Petroleum Industry Bill 2008**, a bill for an Act to revolutionise the Nigerian petroleum industry. If passed, the complexion of Nigerian fiscal regime relative to petroleum operations will be markedly changed. However, it is feared that the Bill will hardly see the light of the day as fierce opposition has trailed its introduction in the National Assembly. The opposition is coming mainly from the international oil companies, whose fortunes are surely to be affected by its passage. For instance, the Bill under its Hydrocarbon Tax Part makes it compulsory for all petroleum operations

companies to pay hydrocarbon tax (which is the present petroleum profits tax under the PPTA) and at the same time to pay corporate tax (which is companies' income tax obtainable under the CITA). This bill is examined in this research with a view to showing its comparative strengths and weaknesses.

However, as identified above it is hoped that this Bill is not negotiated and compromised along the line of legislative process. This point is imperative when it is considered against the backdrop of the recently passed **the Nigerian Oil and Gas Industry Content Development Act**. This Act aims to entrench and encourage the development and participation of Nigerian professionals in the oil and gas sector. It appears the Act has been sold to the National Assembly as a Greek gift, against the obviously more comprehensive and encompassing Petroleum Industry Bill, which itself has a whole Part on Local Content Development. Thus, the National Assembly should have wisely jettisoned and thrown away the Content Bill, now Act, and focused its attention and energy on giving Nigerians a more beneficial law, which the PIB 2008 holds the ace and promise.

As can be seen the issues which the research will confront are steaming hot and needed a surgical blade like incision, so that the issues are kept in proper perspective. The end of the enquiry will be to show the efficacy of the fiscal laws which relate and govern petroleum operations in Nigeria.

1.7 ORGANISATION OF THE RESEARCH

The Research is a six Chapter work. Chapter One covers the general introduction, and deals with such issues as research problems, objective of the research, scope of the research, methodology of the research and literature review. For example, one of the problems which the research aims to dissolve is whether the extant fiscal laws with respect to petroleum operations in Nigeria are potent enough to ensure that the government generates sufficient revenue and thereby build formidable foreign reserve which will enable the government to develop its untapped and neglected agricultural potentials, its manufacturing sector, and its infrastructural framework in order to build an economy, nay a society where her people will have comparable and meaningful standard of living.

Chapter Two is concerned with the Nigerian Petroleum Industry. It traces the nature of petroleum, its formation and its relevance (advantages) as a multifaceted product with variety of uses. The history of the Nigerian petroleum industry was equally x-rayed. The role of the NNPC in the development of the Nigerian petroleum industry was given appropriate treatment. The structure of the petroleum operations in Nigeria was treated, and this is said to be in two broad categories: upstream and downstream operations sectors. More significantly the proposed petroleum industry reform was examined. This was undertaken against the Petroleum Industry Bill 2008 before the National Assembly and the activities of the Petroleum Products Pricing and Regulatory Agency. Additionally, the various laws that underpin petroleum operations in Nigeria were examined. Some of the laws

include the Petroleum Act, the Petroleum Profits Tax Act, Companies Income Tax Act, and the Federal Inland Revenue Service (Establishment) Act, etc.

Also examined in the Chapter were various contractual arrangements in the industry which joint venture, production sharing contract and sole risk arrangements. Finally the Chapter considered ownership and environmental issues, including the issue of militancy, which has relatively abated following the success of the amnesty deal of the Federal Government. Further, the newly enacted **Nigerian Oil and Gas Industry Content Development Act 2010** was given a bird's eye perspective within the context of the research.

In Chapter Three, the relevant fiscal regime of the upstream petroleum operations sector was considered in greater detail. The fundamental law regulating the fiscal aspects of upstream petroleum operations in Nigeria is the Petroleum Profits Tax Act (PPTA). This law is supplemented by Deep Offshore and Inland Basin Production Sharing Contracts Act (the PSC Act) and the Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Act (the Incentives Act). Under the PPTA only the upstream petroleum operations companies are within its purview. However, under the PIB, such companies will be subject to CITA, which presently governs the fiscal activities of downstream operations companies. Although an upstream company may be involved in transportation of oil by ocean going tankers, they do not constitute petroleum operations within the definition of the PPTA as to bring them within the intendment of the PPTA. The PSC, governed by the PSC Act, is an improvement over the Joint Venture arrangement. The Act regulates activities of companies that go into production sharing contract with the NNPC. Despite this, the PSC Act has its shortcomings. On the other hand, the Incentives Act

grants sheepishly and outlandishly generous incentives to the NLNG, which arrangement under the Act is regrettably skewed against the Nigerian people.

Further Chapter Four is concerned with the fiscal regime that regulates downstream operations companies. The principal legislation here is the Companies Income Tax Act 2004, the Companies Income Tax (Amendment) Act 2007 and the Federal Inland Revenue Service (Establishment) Act 2007. The CITA provides the tax regime for all companies in the downstream sector and for upstream companies that are engaged in transportation activities. The principal enactment is the 2004. The 2007 amendment brought some far reaching changes in the existing law. For instance, it concretised the issue of self assessment, and made it compulsory. The attraction of self-assessment, that is one percent filing bonus, was removed, while whole or part payment was retained. Moreover, tax incentive has become a regular feature of taxing statutes, yet its efficacy is much doubted where basic infrastructural amenities are lacking and the political milieu is adversely oriented towards the investor.

In Chapter Five, the issue of administration and enforcement of the fiscal laws that regulate petroleum operations were considered. This is because to be able to assess the efficacy of the laws, it must be considered against the backdrop of how they are administered and enforced. Here the extant law is the FIRS Act. The FIRS Act revolutionised tax administration and enforcement in Nigeria as it conferred novel and far reaching powers upon the FIRS to aid its statutory roles of assessing and collecting due taxes from all companies, whether upstream or downstream petroleum operator. Thus there is introduced such novel provisions as the power to request a banker for information concerning the activities of its customer, the power to require a

person to account for the source of his income, where his style of living does not correlate with his income, the power to enter any premises and search for the purpose of generating evidence, etc. However, innovative as the FIRS provisions are, there appears to be some provisions which are fit and proper for the books than for enforcement. One of such provisions is the distraint powers which the law vests on the FIRS.

Finally, Chapter Six contains the summary, conclusions and recommendations. One of the inferences which flowed from the research is that the presidential power to waive tax is an invitation to abuse, as it will be exercised in favour of president's men, either as favours or settlement. Among others, it has been suggested that the government needed to focus on developing the nation's physical infrastructure, creating a stable investment climate where security is assured, if it must generate optimum results from petroleum operations.

CHAPTER TWO

THE NIGERIAN PETROLEUM INDUSTRY

2.0 INTRODUCTION

Statutorily[11] the word, 'petroleum' means mineral oil (or any related hydrocarbon) or natural gas as it exists in its natural state in strata, and does not include coal or bituminous shales or other stratified deposits from which oil can be extracted by destructive distillation. It also includes motor spirit, gas oil, diesel oil, automotive gas oil, fuel oil, aviation fuel, kerosene, liquefied petroleum gases and any lubrication oil or grease or other lubricant.

Literally, petroleum is a naturally occurring oily, bituminous liquid composed of various organic chemicals that is believed to have formed in deep sedimentary beds from animal and vegetable debris. In other words, it is the petrified and liquefied remains of millions of years' accumulation of decayed animal and plant life. Put in another way, it is a hydrocarbon, which consists of hydrogen and carbon that may exist in gaseous, liquid, or solid forms. In liquid form, it is referred to as crude oil; while in solid form it is called bitumen, tar, pitch, or asphalt. Thus, when we talk of petroleum, strictly speaking, other forms of hydrocarbons are covered.[12]

As to how petroleum is formed, it starts under the Earth's surface by the decomposition of marine organisms. The process of the formation of petroleum is a long drawn one and has been outlined in the following words:

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[11] Section 15, Petroleum Act, CAP 350 LFN 1990; P10 LFN 2004.
[12] But in this Research, a reference to petroleum shall mean a reference to petroleum in its liquid form (i.e., crude oil, or natural gas, which comes along with the liquid or solid form of petroleum).

> the remains of tiny organisms that live in the sea—and, to a lesser extent, those of land organisms that are carried down to the sea in rivers and of plants that grow on the ocean bottoms—are enmeshed with the fine sands and silts that settle to the bottom in quiet sea basins. Such deposits, which are rich in organic materials, become the source rocks for the generation of crude oil. The process began many millions of years ago with the development of abundant life, and it continues to this day. The sediments grow thicker and sink into the seafloor under their own weight. As additional deposits pile up, the pressure on the ones below increases several thousand times, and the temperature rises by several hundred degrees. The mud and sand harden into shale and sandstone; carbonate precipitates and skeletal shells harden into limestone; and the remains of the dead organisms are transformed into crude oil and natural gas. [13]

After formation, the petroleum, being less dense than the surrounding water, would be expelled from the source beds and migrated upward through porous rock such as sandstone and some limestone until it was finally blocked by nonporous rock such as shale or dense limestone. In this way, petroleum deposits came to be trapped by geologic features caused by the folding, faulting, and erosion of the Earth's crust. The trapped petroleum[14] is what forms and constitutes a reservoir[15] of petroleum. Chemically, the composition of all petroleum is hydrocarbons. However, petroleum can and do contain other chemicals, such as sulphur or oxygen. These are as impurities, which tend to affect the commercial values of the particular petroleum product. According to the learned author, crude are classified with reference to the level of impurities it contains – hence a crude oil with a lot of impurities of about 7% sulphur content is referred to as a “sour” crude, while one with comparatively little sulphur content of about 0.5% is called a sweet crude. [16]

The formation of petroleum is as interesting as the history of its discovery. Thus, the surface deposits of petroleum, it has been documented, have been known to man for thousands of years. In the earliest twilight of its discovery, crude oil was long used for

[13] Omorogbe Y., Oil and Gas Law in Nigeria, Lagos: Malthouse Law Books, 2001, pp. 7-9; "Petroleum Production." Encyclopædia Britannica. Ultimate Reference Suite. Chicago: Encyclopædia Britannica, 2009; “Petroleum”, Microsoft® Encarta® 2008. © 1993-2007 Microsoft Corporation.

[14] ibid

[15] Certain terms are used to identify the nature and form of pressure which is needed to force the oil up from the reservoir. For instance, we have the “primary reservoir drive”, “secondary recovery”, and “enhanced oil recovery”. See 1.7 Operational Definition of Terms above.

[16] Per **Omorogbe Y., op cit, p.2**.

limited purposes, such as caulking boats, waterproofing cloth, and fuelling torches. During the Renaissance, which began in the 14th century, some surface deposits were being distilled to obtain lubricants and medicinal products. It was not until the 19th Century that the real exploitation of crude oil began, principally due to increased demand for rock oil. This was the era of Industrial Revolution that brought about a search for new fuels, and the social changes it effected produced a need for good, cheap oil for lamps; people wished to be able to work and read after dark. Meanwhile, whale oil, however, was available only to the rich, tallow candles had an unpleasant odour, and gas jets were available only in then-modern houses and apartments in metropolitan areas. In order to satisfy the demand, various scientists in the mid-19th century started developing processes to make commercial use of crude oil.

Apart from the encouraging efforts of the British entrepreneur James Young, who with others, began to manufacture a variety of products from petroleum, there were commendable efforts from other climes. Thus in 1852 Canadian physician and geologist Abraham Gessner obtained a patent for producing from crude oil a relatively clean-burning, affordable lamp fuel called kerosene; and in 1855 an American chemist, Benjamin Silliman, published a report indicating the wide range of useful products that could be derived through the distillation of petroleum.[17]

From this period onwards, the quest for greater supplies of crude oil began. It had been a common knowledge, at this time, that wells drilled for water and salt were occasionally infiltrated by petroleum. This however gave birth to the concept of drilling for crude oil itself. From 1857 to 1859 the first oil wells were dug in Germany. Several historical events accounted for the origin of the oil but significantly, it has been claimed that the event:

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[17] "Petroleum" Microsoft, Encarta, 2008.

> that gained world fame was the drilling of an oil well near Oil Creek, Pennsylvania, by "Colonel" Edwin L. Drake in 1859 (who was) contracted by the American industrialist George H. Bissell—who had also supplied Silliman with rock-oil samples for producing his report—drilled to find the supposed "mother pool" from which the oil seeps of western Pennsylvania were assumed to be emanating. The reservoir Drake tapped was shallow—only 21.2 m (69.5 ft) deep—and the petroleum was a paraffin type that flowed readily and was easy to distil.[18]

Thus it can be safely asserted that the growth of the modern petroleum industry was a consequence of Drake's drilling success. Secondly, following the invention of the automobile and the gaping energy needs foisted by World War I of 1914 to 1918, one of the basic foundations of any industrial society today remain the petroleum industry. This is amplified by the importance of petroleum, which rank it first among other energy sources. Thus the modern industrial societies use it primarily to achieve a degree of mobility—on land, at sea, and in the air—that was barely imaginable less than 100 years ago.

In addition, petroleum and its derivatives are used in the manufacture of medicines and fertilizers, foodstuffs, plastics, building materials, paints, and cloth and to generate electricity. In fact, modern industrial civilization depends on petroleum and its products; the physical structure and way of life of the suburban communities that surround the great cities are the result of an ample and inexpensive supply of petroleum. In addition, the goals of developing countries—to exploit their natural resources and to supply foodstuffs for the burgeoning populations—are based on the assumption of petroleum availability. In recent years, however, the worldwide availability of petroleum has steadily declined and its relative cost has increased. Many experts forecast that petroleum will no longer be a common commercial material by the mid-21st century.[19] More recently, it has been emphatically submitted that oil and gas supply is essential to sustaining economic growth in the industrialized world and is key to progress in nations working their way towards

[18] "Petroleum" Microsoft, Encarta, 2008.
[19] "Petroleum", Microsoft, Encarta, 2008 (DVD).

prosperity. Thus "the demand for oil and gas will continue to increase, as they are expected to remain the leading energy sources for some time to come".[20] In the same vein, it has been added that petroleum is an extremely versatile commodity with very many industrial uses. Its importance however lies in the fact that crude oil and natural gas are the most important sources of energy in the world today. It is true to say that the use of petroleum as an energy source made the twentieth century what it was.[21] From the above overview of petroleum from global historical perspective, the question is apt to be asked, how does Nigeria come into the scheme of unfolding direction of the world energy order? This now leads to a consideration of the history of the Nigerian petroleum industry.

2.1 HISTORY OF NIGERIAN PETROLEUM INDUSTRY

Just as seen above with respect to global historical perspectives underpinning the world petroleum industry, the history of petroleum operations in Nigeria predates modern day independent Nigeria. Therefore, the history of petroleum operations in Nigeria, in this Research, shall be considered in phases – the first phase covering the periods of 1900 to 1959; and the second phase covering the period 1960 to date.

[20] **Longwell, H.J., "The Future of the Oil and Gas Industry: Past Approaches, New Challenges"**, The World Energy, Vol. 5 No. 3, 2002, pp. 100-104 at 101. See also http://www.worldenergysource.com/articles/longwell-WE-v5n3.pdf
[21] **Omorogbe, Y. op. cit, at p. 3**

2.1.1 FIRST PHASE – 1900 to 1959

The need for energy to sustain the engine of industrial revolution led to oil rush, which inevitably meant that the commodity must be sought for wherever it might be found. Thus, the advent of the (Nigerian) oil industry has a nexus with the upsurge in oil exploration activities following the Drake's success story.[22] Consequently, the history of the Nigerian petroleum industry can be traced to 1908, "when a German entity, the Nigerian Bitumen Corporation"[23], began, unsuccessfully, exploration activities in the Araromi Area, West of Nigeria[24], albeit these pioneering efforts were abruptly disrupted by the outbreak of the World War I in 1914.[25] But according to **Omorogbe,** the Nigerian legislation on petroleum had existed for about a decade before exploration was first undertaken. The first piece of legislation was the Petroleum Ordinance of 1889, which was followed by the Mineral Regulation (Oil) Ordinance of 1907, both of which laid down a basic framework for the development of petroleum and its natural resources.[26] However, "the major constituents of the laws which touch upon the exploration and production of petroleum date back to the Mineral Oils Act of 1914 which was enacted to regulate the right to search for, win and work mineral oils".[27] Despite the seeming inconsistency in the position of the two authors, the common ground as between the learned authors is that the statutory environment predated the actual exploration and production activities regime as far as petroleum operations are concerned in Nigeria.

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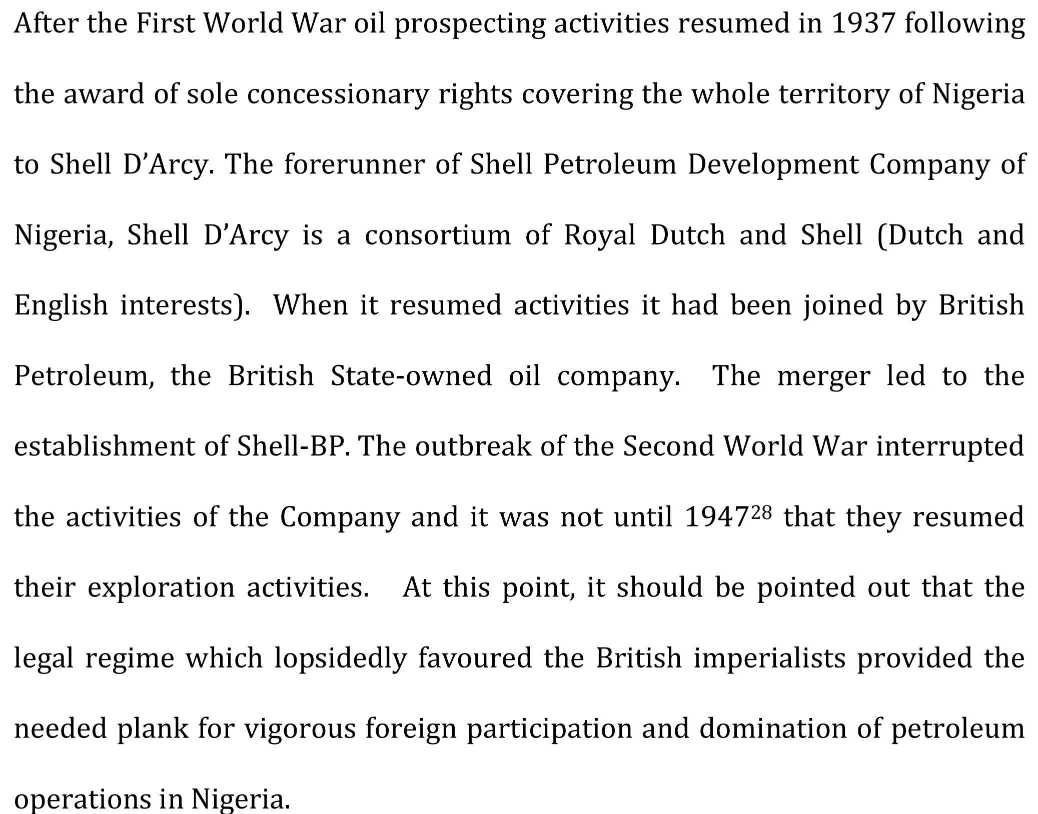
[22] See n. 15 above.
[23] Omorogbe Y., op cit., p. 17, rendered it as **German Bitumen Company**.
[24] The place forms part of the present day Ondo State.
[25] http://www.nnpcgroup.com/development. .
[26] **op cit. p. 16**
[27] Etikerenste G., Nigerian Petroleum Law, second edition, Dredew Publiishers, 2004, p. 6



After the First World War oil prospecting activities resumed in 1937 following the award of sole concessionary rights covering the whole territory of Nigeria to Shell D'Arcy. The forerunner of Shell Petroleum Development Company of Nigeria, Shell D'Arcy is a consortium of Royal Dutch and Shell (Dutch and English interests). When it resumed activities it had been joined by British Petroleum, the British State-owned oil company. The merger led to the establishment of Shell-BP. The outbreak of the Second World War interrupted the activities of the Company and it was not until 1947[28] that they resumed their exploration activities. At this point, it should be pointed out that the legal regime which lopsidedly favoured the British imperialists provided the needed plank for vigorous foreign participation and domination of petroleum operations in Nigeria.

Thus, it was expressly provided that grants to search for and win oil could only be made to British subjects and to those companies which had their principal places of business in Britain or in its dominions and whose chairmen or majority shareholders and directors were British subjects.[29] This amounted to naked denial of participatory, control or ownership rights in the management of such companies to Nigerians by the colonial predators. The Nigerian Government, through the Nigerian National Petroleum Corporation, is adapting a conscious policy of local content, and has in fact Nigerian Content Division, which aims to bolster indigenous participation in petroleum operations in Nigeria, and develop local manpower and expertise thereto.

[28] Etikerentse G., ibid, stated the resumption date to be 1946. The concession was an oil exploration licence that covered the entire mainland of Nigeria (i.e. 375,000 square miles).

[29] The indigenisation policy of the Federal Government halted this trend, when BP's shares were nationalised in 1979.

While ownership, control and operation of the companies who are subject to grant of exploration and mining rights reside in foreigners (specifically British entrepreneurs or companies incorporated in Britain), the property in and control of all mineral oils on under or upon any land in Nigeria and of all rivers, streams and watercourses throughout Nigeria vested in the British Crown.[30] Successively thereafter, the regime of state control and ownership of all minerals persisted. Presently, **Section 44(3) of the Constitution of the Federal Republic of Nigeria 1999**[31] provides that the entire property in and control of all minerals, mineral oils and natural gas in under or upon any land in Nigeria or in, under or upon the territorial waters and the Exclusive Economic Zone of Nigeria shall vest in the Government of the Federation and shall be managed in such manner as may be prescribed by the National Assembly. The legal regime which vests ownership[32] in the Federal Government has been a subject of disputes and militancy within the Niger Delta region of Nigeria,[33] and has drawn questions to be asked, whither fiscal federalism?[34]

Meanwhile, Shell-BP continued with its exploration activities, so that in 1951 it successfully drilled its first well "at a location near Ihuo village, some sixteen kilometres north-east of Owerri. From there its operations were moved to drill its Akata-I well.[35] The Shell-BP had a field day as far as the development of the Nigerian petroleum industry was concerned. Shell was able to leisurely

[30] Section 3(1) Minerals Act 1946. Moreover, the Mineral Oils (Amendment) Act 1950 in section 10 extended state ownership and control of all minerals to include the submarine areas of Nigeria's territorial waters.
[31] See also section 1 Petroleum Act CAP 350 LFN 1990; CAP P10 LFN 2004;
[32] See p. 64, infra.
[33] See page 65, infra.
[34] "Niger Delta: What happens to fiscal federalism?" Sunday Magazine, Sunday Champion, June 21, 2009, pp. 15-17. See page 64, infra.
[35] Etikerentse G., op cit. p. 7.

explore and select choice acreage until 1962, by which time it retained 15,000 square miles of the original concession area.[36] In fact, stated that Shell enjoyed a great measure of governmental protection and the early development and growth of Nigerian petroleum law were understandably linked with Shell-BP operations and advancement.[37] However, one wondered why Shell-BP did not proactively, or rather instinctively and instructively, begin with a core value of socially responsible behaviour, and environmentally sound practices. Till date Shell has been at loggerheads with the people of the Niger Delta over the manner it carries its operations in the region. Many cases have been brought before the courts which bordered on environmental pollution. Restiveness and militancy have taken a new twist following piled up cases of mistreatment by Shell-BP and other operators in the region. For instance, following a suit filed under **Alien Tort Claims Act 1789**, recently in far away New York, Shell-BP agreed to an out of court settlement to pay US$15,500,000.00 in damages to the Ogoni peoples.

Notwithstanding the measure of freedom which Shell-BP enjoyed, the government took steps to ensure that Shell-BP complied in its operations to safe and good oil-field practices, which benchmarked international standards as then obtained in the industry. Thus, a set of regulations, made pursuant to powers granted by section 9 of the Mineral Oils Act 1914 known as **The Mineral Oils (Safety) Regulations 1952** were issued. Later it was replaced by the **Mineral Oil (Safety) Regulations 1963**, though it was retroactively to

[36] **Omorogbe Y. op cit. p. 17**
[37] **Etikerentse G., ibid**

have effect from 11th April 1962. Currently, the Regulations as amended are known as Mineral Oils (Safety) Regulations and forms.[38]

The efforts of Shell-BP paid off when in 1956 it made its first commercial discovery in a location near Oloibiri in present day Bayelsa State, with a production capacity of 5,100 barrels per day in 1958. Swiftly, the government took steps to enact the **Oil Pipelines Act of 1956 (CAP 145 of the 1948 Edition of the Laws of Nigeria)**. The passage of this law is understandable, since pipelines remain "the cheapest means of transporting crude oil through long distances between the well head and the point of exportation or refining".[39] In other words the law was meant to square up with the exigencies of Shell-BP's operations. Further, the government took steps to protect its fiscal interests in the petroleum industry by enacting a law to tax specifically "the realised profits of oil companies, separately and distinctly from the companies which engage in other enterprises. For instance, the **Petroleum Profits Tax Act was passed in 1959** to retroactively take effect from 1st January 1958. The Act is now known as CAP 354 LFN 1990; CAP P13 LFN 2004.[40]

Shortly before independence, the obnoxious provision which limits the grant of exploration licences to only British companies was repealed. Accordingly in 1959 and by virtue of the **Mineral Oils Act (CAP 120 of the 1958 Edition of the Laws of Nigeria)**, the sole concessionary rights granted to Shell-BP were reviewed and "various rights were extended to other companies of various

[38] A subsidiary legislation of the Petroleum Act, CAP P10 LFN 2004.
[39] Etikerentse G., op cit. p. 8.
[40] This and other laws which determine the fiscal regime of petroleum operations in Nigeria are discussed in Chapters 3, 4 and 5.

nationalities."[41] The list of the companies which were granted licences, at the time, included the Nigerian Gulf Oil Company, a subsidiary of Gulf Corporation (now Chevron). Other multinational corporations which secured exploration licences about this time included "Mobil Oil, Texaco, Sunray-Tenneco, Occidental, Agip, the Italian state-owned oil company as well as its French counterpart, Safrap, which later became known as Elf Petroleum".[42] Despite the entry of other participants into the playing field, Shell remains "the largest producer of Nigeria oil", due to its inherited monopolistic position, and "about eighty percent of all existing concessions are held by Shell and half of Nigeria's oil is produced within these arrangements".[43]

2.1.2 SECOND PHASE 1960 – TO DATE

Pioneer production of crude oil began in 1958 from Shell-BP's oil field in Oloibiri, that "by late sixties and early seventies, Nigeria had attained a production level of over 2 million barrels of crude oil a day".[44] According to the Nigerian National Petroleum Corporation (hereafter, the NNPC), "production figures dropped in the eighties due to economic slump, 2004 saw a total rejuvenation of oil production to a record level of 2.5 million barrels per day. Current development strategies are aimed at increasing production to 4 million barrels per day by the year 2010".[45] This figure was less than the production of 2.5 million barrels recorded in 2004.

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[41] Omorogbe, op cit., p.17. According to Etikerentse, G. ibid, "available for grant in addition to other areas was 50% of Shell's entire concession…, which it had relinquished in 1958".
[42] Etikerentse G., ibid.
[43] Omorogbe, Y., ibid.
[44] http://www.nnpcgroup.com/history. See generally, Ownership/Community Issues, infra.
[45] see **Nigeria's oil output dips by 35m barrels in** "The Nation Energy", The Nation Newspaper, Tuesday, June 16, 2009, p. 31

But attacks on oil facilities by the militants in the last three years have substantially dramatically cut Nigeria's oil output. The output had since dropped from 2.4 million barrels per day to 1.6 million and lately to 1.8 million but with the current onslaught, the daily output may dip below 1.6 million barrels.[46] It has been stated that as at January 2009 by DPR that "the country's proved and probable reserves were put at 32.71 billion barrels"[47] But compare this with NNPC's estimates of 32.5 billion barrels of proven oil reserve and 187 trillion cubic feet of gas reserves.[48]

This means that government projected production is an unrealistic goal, nay dream. For instance, the Department of Petroleum Resources, Nigeria's oil and gas industry regulator, stated at its 2009 first quarter media briefing in Lagos that "oil production in the first two months of this year – January and February – averaged 2,008,132 and 2,024,418 barrels per day" By now there was no doubt that Nigeria is oil producing nation, with massive reserves. This era undoubtedly witnessed, and is still witnessing, the highest number of activities as it is within this era that oil took the centre stage as the main stay of the Nigerian economy. Efforts appear geared towards reversing this trend.

Thus, it has been emphasized that there was the "need to reposition non-oil tax revenues as the number one source of sustainable revenue for national development (through) tax reform initiatives at all tiers of government.[49] As a testimony to this, the existing petroleum legislation (that is **Mineral Oils Act**

[46] The Nation Newspaper of Tuesday June 23, 2009 at page 32
[47] The Nation Energy", The Nation Newspaper, Tuesday June 16, 2009, p. 31.
[48] see, http://www.nnpcgroup.com/upstream opportunities.
[49] Remi Babalola, Minister of State of for Finance, **"Boosting Government Revenue through Non-Oil Taxes"**, at the 11TH Annual Tax Conference of the Chartered Institute of Taxation of Nigeria, held at the NICON Luxury Hotel, Abuja, 7th May 2009: http://www.fmf.gov.ng/downloads/speeches_in_pdf/boostgoverrev070509.pdf.

1914 and its amendments) was repealed by the Petroleum Act 1969.[50] The 1969 Act was the first major attempt at "producing a detailed and comprehensive law for the grant of rights to search for and win oil in Nigeria." Naturally this law gave rise to other instruments[51], while repealing the 1914 Act, contained hitherto in CAP 120 of the 1958 Edition of the Laws of Nigeria.[52] However, without this provision, and assuming the Act was silent as to the position of the 1963 Regulations under the regime of the Petroleum Act, it is submitted that the Regulations would still be applicable as an extant law under the enactment. This is because where an enactment is repealed and another enactment is substituted for it, then - any subsidiary instrument in force by virtue of the repealed enactment shall, so far as the instrument is not inconsistent with the substituted enactment, continue in force as if made in pursuance of the substituted enactment.[53]

Further in the early stages of this, precisely 1970s, Nigeria began to create institutional framework for direct government participation in petroleum activities. This was inevitable because, albeit "the principal Nigerian legislation on petroleum dates back to the very early part of last century…, yet no real discernible government policy on petroleum existed".[54] The learned author adduced reasons for the absence of a policy framework, to wit there had been no substantial production of oil in the 1970s; and the mainstay of the economy, then, was agriculture so that "government's interest in petroleum

[50] Now CAP 350 LFN 1990; CAP P10 LFN 2004.
[51] For instance, **Petroleum (Drilling and Production) Regulations** prescribed under Legal Notice No. 69 of 1969. According to Omorogbe Y. ibid, the regulations" laid down what continues to be the foundation of the legal framework for the regulation of the oil industry in Nigeria.
[52] See section 14(2) CAP P10 LFN 2004. However, see paragraph 4 of Schedule 4 to the Petroleum Act that saves the **Mineral Oils (Safety) Regulations 1963.**
[53] **Section 4(2)(c) Interpretation Act CAP 192 LFN 1990; CAP I23 LFN 2004**,
[54] Etikerentse, G., op cit. p. 16.

was limited to enforcing the few petroleum regulations that existed (and) mere collection of taxes from the oil companies".

With respect, the position of the learned author is not completely tenable. One, according to the official website of the NNPC, "by the late sixties and early seventies, Nigeria had attained a production level of over 2 million barrels of crude oil a day", so that it is tantamount to half truth to submit that there was "no substantial production of oil in the 1970s". Second, the legal environment was just smarting out from the imperialist regime which orchestrated a culture of economic domination of the natives, when it restricted participation to British corporations. This point the learned author emphasized when he stated that Nigeria "was caught in the web of what was termed the old international economic order, whereby "the investment for the exploitation of natural resources of developing third world countries were totally in the hands of transnational corporations". Shortly after independence, Nigeria was plunged into civil war, which meant that the attention of the government was directed at prosecuting the civil war.

Three, the transnational corporations had the capital, technology and management expertise and resources needed for the exploitation of an extractive mineral like petroleum; and with these credentials "they were granted awards of oil mining concessions for extended periods of time".[55] Basically, the absence of governmental policy was the result of interplay of many factors, which include the unfavourable legal regime which transited into the new independent Nigeria, the civil war, absence of technical knowhow and government's pre-occupation with its mainstay, then, agriculture.

[55] Etikerentse, G., op cit. p. 17.

Aside from the above considerations, it has been submitted that certain remote and immediate factors hastened the actual participation of the Nigerian Government in the activities of the Nigeria-based transnational corporations, and thus in the oil and gas industry.[56] These factors, in brief, include –

(a) Nigeria realised that a change in the contractual status quo in which the transnational petroleum corporations virtually owned and controlled extracted petroleum was imperative[57]. No wonder, the Second National Development Plan, 1970-1974 expressly noted that the interest of the foreign private investors cannot be expected to coincide with national aspirations, and thus emphatically declared that *the government will seek to acquire, by the law of necessity, equity participation in a number of strategic industries that will be specified from time to time. In order to ensure that the economic destiny of Nigeria is determined by Nigerians themselves, the government will seek to widen and intensify its positive participation in industrial development*.

Thus the offshoot of this factor or reason is more deeply ingrained than painted above. For instance, the Nigerian Enterprises Promotion Decree (NEPD) 1972 excluded non-Nigerians from participation in certain categorized businesses (contained in Schedule 1 of the Decree) and restricted their participation in favour of Nigerians in others. Schedule 2 contained the ventures in which non-Nigerians may participate but not less than 60% of the equity holding must be reserved for Nigerians, and Schedule 3 listed businesses of which not less than 40% equity holding must be reserved for Nigerians. Thus this assertive action of the government is not restricted to the

[56] Etikerentse, G. op cit. pp.17-19.
[57] Ibid.

petroleum industry alone. However, it must be noted that following the enactment of the **Nigerian Investment Promotion Commission (NIPC) Act CAP N117 LFN 2004** the Nigerian investment climate has been liberalised to the extent any person (whether Nigerian or non-Nigerian) may participate in any enterprises as far as such enterprises do not fall under those prohibited by law. Those prohibited by law, otherwise known as the Negative List.[58]

(b) Greater impetus was added by the demand of other third world countries with similar experiences for "a change in the then existing international economic order, (while) the corridors of the United Nations reverberated with the sounds of the demands by the third world nations" for unconditional reordering of the old international economic order. The demands paid off with the passage of a United Nations Resolution on Permanent Sovereignty over Natural Resources"[59]

(c) Notwithstanding the enactment of the Petroleum Act in 1969, it was discovered that the country's earnings from petroleum production had not increased to any appreciable extent. In short, it would appear that the Act only reduced the primary term of an oil mining lease to twenty years from thirty and forty years which were previously obtainable.

(d) In 1971 the government reacted positively to pressure mounted upon it to effect a change. Thus, it began to participate in, and acquire, the operations of the transnational oil corporations in Nigeria.[60] It has been pointed out that, "in the case of the upstream petroleum companies, government acquisition did

[58] see **Sections 17, 18 and 31 NIPC Act CAP N117 LFN 2004.**

[59] GA Res. 1803, 17 UN GAOR, Supp. (No. 17) UN Doc. A/5217 (1962): the resolution recognized the sovereign rights of the host communities to the ownership of natural resources in their territories.

[60] See note 49, page 22 above. To do this, the Nigerian Enterprises Promotion Acts 1972 No. 4 and 1977 No. 3 were passed respectively. Now repealed, the Acts divested the ownership of affected companies, in favour of Nigerians, from the foreigners.

not extend to the ownership of the shares in the companies, but just in their operations".[61] This point is very important. One, it means that the government was not a shareholder in such upstream companies, and would not look to the profits of the companies in the form of dividends. Two, the nature of government's acquisition with respect to downstream companies was in the ownership of the shares in the affected companies, and would enjoy the rights that ordinarily vests in any shareholder[62]. Three, the relationship of the government and the upstream companies were one of partnership, and not master/servant or principal/agent.

(e) By January 1970, the civil war ended. The government initiated the three Rs of Reconstruction, Rehabilitation and Reconciliation as a way to overcome the effects of the war. Thus government needed funds to implement two of the three Rs – that is, reconstruction and rehabilitation.

With these factors present, the government plunged into the mainstream activities in the petroleum industry. In order to achieve this, it adopted the paradigm institutional framework, leading to the creation of a national oil corporation. National oil corporations have always been a feature of the oil industry the world over. It probably originated from Europe. Just like the Nigerian experience, ownership even in Europe took the form of share acquisitions. For instance, in 1914 the British government acquired majority shares in the Anglo-Persian Oil Company (now known as British Petroleum). The Latin American countries led the way in the formation of NOCs, the very first being Yascimientos Petroliferos Fiscales of Argentina (YPF) formed in 1922. Save for only few other developing countries (for instance Mexico whose NOC,

[61] Etikerentse, G., op cit. p. 19.
[62] For instance, right to notice of meeting, right to vote, and right to dividend.

Petroleos Mexicanos (PEMEX) was active in 1938 due to Mexican nationalisations and the National Iranian Oil Company formed in 1957 to give effect to the nationalisation of the Anglo-Iranian concession) "all other national oil corporations in developing countries were created after the establishment of OPEC in 1960".[63]

ESTABLISHMENT AND GROWTH OF NATIONAL OIL CORPORATION

The established practice amongst oil producing nations is to establish statutory bodies charge with responsibility over the exploitation and exploration activities including end-point stage activities (for instance, refining, marketing and distribution). This is known as national oil corporations. The NNPC is the Nigerian national oil corporation (NOC) [64]. NOCs are created to (1) to ensure that the state has constant access to oil so that its energy supplies will not be impeded. On this one wonders the extent to which the NNPC has translated this motivation to reality in the case of Nigeria. Recently, the country experienced acute shortage of refined petroleum products; while the activities of the militants in the Niger Delta continue to impact negatively on the country's production capacity; to oversee and control the activities of the domestic oil industry. It may be said that the NNPC has averagely done well here as regards increased exploration, sustaining effective state participation and promotion of investments in the sector. However, the capacity of the NNPC has been eroded by the militants, that today there is a permanent military and paramilitary post in the Niger Delta region of Nigeria, known as the Joint (Military) Task Force (JTF) on the Niger Delta. Frequent clashes between the JTF and the militant group, Movement for

[63] Omorogbe, Y., op cit., pp. 96-99.
[64] Omorogbe Y., op cit. pp.97-98.

Emancipation of Niger Delta (MEND) have left the Nigerian oil industry gasping for survival.

Another reason for the NOC is to make profits for the state. The response to the performance of the NNPC as regards this reason can be found in the report of the United Nations which says that "despite hundreds of billions of dollars in oil revenue, about 70 percent of Nigeria's population of 140 million live on less than $2 per day, (even as) the World Bank estimates that about $300 billion of government oil funds are unaccounted for. Also, in a recent audit of oil revenues by the Nigeria Extractive Industry Transparency Initiative, which covered the period between 1999 and 2004, it was discovered that there were many sharp practices at different points of the industry.[65]

Further, in this phase of the history of the Nigerian petroleum industry, it has been rightly stated that "1971 was a critical year for oil industry", following the establishment of the Nigerian National Oil Corporation (NNOC) in April of that year.[66] Etikerentse who attempted to trace the origin of the Nigerian National Petroleum Corporation (NNPC) posited that "there is paucity of clear facts relating to the genealogy of the governmental agencies which constituted predecessors of the present NNPC".[67] Two views have been advanced regarding the historical origin of the NNPC. One view is that it started as the petroleum section of the Federal Ministry of Finance and that the government's regulatory role in the petroleum sector was by the defunct Ministry of Mines and Power. However the second view holds that it began as an offshoot of a one man unit in the Mines Division of the then Ministry of Lagos Affairs, beginning from 1958. Later, the unit

[65] see http://www.neiti.org.ng/news/VOA1707/pdf
[66] Omorogbe Y., op cit. p. 17.
[67] Etikerentse, G., ibid p. 19.

was elevated to a full petroleum division in that ministry in 1963. This was in response to increased activities in the petroleum industry.

Other activities followed the creation of this division, and this was captured, at the risk of length, by the learned author below:

> The Petroleum Division later expanded to the status of a Department – that of Petroleum Resources in 1970 under the Ministry of Mines and Power as more personnel were attracted to meet the increased demand of a booming oil industry. In 1975, the Petroleum Resources Department was yet again upgraded and it became known as the Ministry of Petroleum Resources one year later, when the Department responsible for nuclear energy was excised from the ministry of Petroleum and Energy. The function of the Ministry of Petroleum Resources until 1971 was mainly the enforcement of regulations relating to the operations of the oil companies in order to ensure their compliance with good field practice. The collection of petroleum profits tax was administered by the Petroleum section of the Ministry of Finance and there was no government participation at all in the activities of the oil companies at that time. Also about the same time, another related governmental agency was about to be born. Spurred by the late Mr. Abdul Azeez Attah who was then the Permanent Secretary in the Federal Ministry of Finance, Nigeria became a member of the Organisation of Petroleum Exporting Countries (OPEC) in 1971, and for the implementation of OPEC's decisions, a governmental agency was necessary. Thus, by April 1971, the Nigerian National Oil Corporation (NNOC) was established by Act No. 18.[68]

The author was quoted extensively in order to provide an objective basis for analysis. The facts to be gathered from the accounts above are simple: NNOC was an offshoot of the then Federal Mines and Power; and NNOC was an offshoot of the NNPC. However, it would appear from the author's submission above that Nigeria joined the OPEC before the establishment of the NNOC. The reverse is the case because NNOC was established in April 1971, and Nigeria joined the OPEC in July 1971. Secondly, as will be seen shortly, there appears to be disagreement as regards the exact Ministry which merged with the NNOC following the enactment of the Nigerian National Petroleum Act.[69]

Thus, by Decree No. 18 of April 1971, the Nigerian National Oil Corporation was established "to engage in prospecting for, mining and marketing oil and all other

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[68] Ibid.

[69] The **Nigerian National Petroleum Act 1977** established the NNPC. The law is now to be found in **CAP 320 LFN 1990; CAP N123 LFN 2004.**

activities with the petroleum oil ministry". According to **Omorogbe Y.,** jurisdictional problems between NNOC and the Ministry of Mines and Power led to the creation of NNPC, which combined the functions of NNOC with the regulatory functions of the Ministry.[70] Another somewhat contradictory was advanced below, to the effect that:

> the NNOC operated alongside the Federal Ministry of Petroleum Resources – the latter limiting its functions to regulating the operations of the oil companies, but because of the dichotomy created by their difference existence and seemingly independent operations, administrative conflicts and ineffective control resulted. (Thus in order to achieve the higher standards of the goals and policies of government in the petroleum industry), the NNOC was merged with the former Federal Ministry of Petroleum Resources to form the NNPC. In doing so, the Act also repealed the NNOC Act of 1971 and dissolved the Federal Ministry of Petroleum Resources.[71]

From the above accounts the contradiction stems from which Ministry, as between the Ministry of Mines and Power and Ministry of Petroleum Resources, was merged with the NNPC. According Etikerentse, the NNOC Act of 1971 was repealed and the Federal Ministry of Petroleum Resources dissolved – all under NNPC establishment Act. However, **section 23(2) of CAP N123 LFN 2004,** the repeal section, provides that "as from the date of commencement of this Act, the Nigerian National Oil Corporation Act 1971 shall stand repealed and, accordingly, the Nigerian National Oil Corporation established under that Act shall be dissolved". Also in **section 22 of the Act**, the word "Minister" interpreted to mean "the Minister of Petroleum Resources."

Thus, under the Act, there was no section which dissolved the Federal Ministry of Petroleum Resources. Of course, the interpretation of the word "minister" and the assignment of roles to him under the Act meant that no dissolution of the Ministry

[70] Op cit. pp. 99-100. The regulatory functions of the NNPC were undertaken by the Petroleum Inspectorate which was established as an integral part of the corporation: see Sections 10-11, CAP N123 LFN 2004.
[71] Etikerentse G., op cit. p. 20.

was envisaged or done.[72] Thus, except the dissolution of the Ministry of Petroleum Resources was by executive fiat, the merger that birthed the NNPC must have been between the NNOC and the Ministry of Mines and Power. This position is to be preferred having regard (a) to the common ground that the NNOC was an offshoot of the Ministry of Mines and Power; and (b) to the fact that there could not have been a Minister of Petroleum Resources under the Act without an appropriate Ministry to take charge and administer.

Transitionally, Part B of Schedule 2 to CAP N123 LFN 2004 vests in the NNPC all NNOC's "assets, funds, resources, moveable and immovable property as well as the liabilities and benefits in NNOC's existing contracts, transactions and causes. These are in addition to its duties which include –

i. Exploring and prospecting for, working, winning or otherwise acquiring, possessing and disposing of petroleum;
ii. Refining, treating, processing and generally engaging in the handling of petroleum for the manufacture and production of petroleum products and its derivatives;
iii. Purchasing and marketing petroleum, its products and by-products;
iv. Providing and operating pipelines, tanker-ships or other facilities for the carriage or conveyance of crude oil, natural gas and other products and derivatives, water and any other liquids or other commodities related to the corporation's operations;
v. Constructing, equipping and maintaining tank farms and other facilities for the handling and treatment of petroleum and its products and derivatives;
vi. Carrying out research in connection with petroleum or anything derived from it and promoting activities for the purpose of turning to account the results of such research;
vii. Doing anything required for the purpose of giving effect to agreements entered into by the Federal Government with a view to securing

[72] For instance, section 1(2) of the Act declares the Chairman of the Board of Directors to be the Minister.

participation by the government or the corporation in activities connected with petroleum;

viii. Generally engaging in activities that would enhance the petroleum industry in the overall interest of Nigeria; and

ix. Undertaking such other activities as are necessary or expedient for giving full effect to the provisions of this Act.[73]

Thus, the duties of the NNPC extend to cover all facets of the petroleum industry: upstream operations, downstream operations and natural gas operations. Further the NNPC was given enormous powers to do anything which in its opinion is calculated to facilitate the carrying out of its duties including, without limiting the generality of the following, the power to –

(a) to hold, manage and alienate movable and immovable property;

(b) to purchase or otherwise acquire or take over all or any of the assets, businesses, properties, privileges, contracts, rights, obligations and liabilities of any other company, firm or person in furtherance of any business engaged in by the Corporation;

(c) to enter into contracts or partnerships with any company, firm or person which in the opinion of the Corporation will facilitate the discharge of the said duties under this Act;

(d) to establish and maintain subsidiaries for the discharge of such functions as the Corporation may determine; and

(e) to train managerial, technical and such other staff for the purpose of the running of its operations and for the petroleum industry in general.[74]

[73] See **Section 5(1) CAP N123 LFN 2004.**

It has been argued that the "very prominent position once occupied in petroleum matters by the NNPC has waned slightly, due to a few reasons". Such reasons include the dependence of the NNPC on the government for its funding, which results frequently in its inability to meet its financial obligations as they fall due; the removal of the Petroleum Inspectorate as an integral part of the NNPC[75] (the Inspectorate is now known as the Department of Petroleum Resources, and reports to the Ministry of Petroleum Resources. The Department is apex regulator of the Nigerian petroleum industry, and this includes regulating the operations of the businesses in which the NNPC is the majority joint venture partner. Under the **Petroleum Industry Bill 2008,** the DPR will metamorphose into **The Nigerian Petroleum Inspectorate**[76]); and the state of some of NNPC's subsidiaries, especially the Refineries. For instance, fuel scarcity has become nearly a way of life of the people, and all the refineries are operationally inept. Today, Nigeria is heavily dependent on imported fuel.[77]

However, notwithstanding the above considerations which, according to the learned author, has had adverse effect on the prominence of the NNPC in the petroleum industry it is indubitable that the Corporation has contributed greatly to the development of the Nigerian petroleum industry. Since its creation, the NNPC has undergone three main reorganisations. The first one was during the first half of the decade of the 1980s following the report of the Irikefe Commission of Enquiry set up to look into the alleged disappearance of US$2.8 billion from the account of the NNPC; the second was in 1988 which culminated in the separation

[74] See **Section 6(1) of the Act**.
[75] See Sections 10 and 11 of the Act.
[76] See **Article 37 of the Bill**
[77] Even the establishment of the **Petroleum Products Pricing Regulatory Agency** in 2003 could not solve the problem, as the country experienced, once again, scathing fuel scarcity in the months of April and May 2009. The Agency was established by virtue of **Petroleum Products Pricing Regulatory Agency Act (No. 8) 2003 and its 2004 Amendment.**

of the Petroleum Inspectorate from the NNPC, and its merger with the Ministry of Petroleum.[78] Petroleum operations in Nigeria are regulated by the Department of Petroleum Resources (DPR), a department within the Ministry of Petroleum Resources. The DPR ensures compliance with industry regulations, processes applications for licences, leases and permits, establishes and enforces environmental regulations. Prominent and important as the role of the DPR stands today, the manner of its emergence by an act of executive fiat must be decried. Thus, by pulling out the Petroleum Inspectorate from the NNPC, and without amending the relevant provisions of CAP N123 LFN 2004 that established the hitherto Petroleum Inspectorate, the executive displayed flagrant disregard to the laws of the land, and must be condemned for what it is – sheer act of executive lawlessness.

The third and major reorganisation occurred in 1995 when the NNPC was restructured into six directorates each headed by an executive director. For instance, the Exploration and Production Directorate which consists of some Strategic Business Units (SBUs); the Refining and Petrochemicals Directorate which consisted of downstream subsidiaries of the NNPC as SBUs[79]; the Engineering and Technical Services Directorate consisted of Pipeline and Tank Construction Division, Research and Development Division; and Engineering and Technical Division, National Engineering and Technical Company Limited (NETCO), and Materials Management Department; the Commercial Investments Directorate, which consisted of Hydrocarbon Services of Nigeria Limited (HYSON) in affiliation with Carlson (Bermuda) Limited, that undertakes petroleum

[78] Omorogbe Y., op cit. pp. 102-106.

[79] For instance, the Port Harcourt Refining Company Limited; the Kaduna Refining & Petrochemicals Company Limited; Eleme Petrochemicals Company Limited; Warri Refining & Petrochemicals Company Limited; and Pipelines and Products Marketing Company Limited.

products marketing in the West and Central African sub-regions; the Finance and Accounts Directorate; and the Corporate Services Directorate. It should be noted that "the Public Affairs Division, Corporate Planning and Development Division, the Corporate Secretariat and Corporate Audit Department are under the office of the Group Managing Director".[80]

Commenting on the third reorganisation, Omorogbe Y. described it "as practical in the sense that entities and departments with similar functions are grouped together within the same directorate." However, he aptly noted an anomalous situation that pervaded the reorganisation exercise. Thus within the reorganised Directorates,

> limited liability companies coexist side by side with internal departments, headed by managing directors and general managers respectively, and are grouped together as divisions. This situation is particularly marked in the Exploration and Production Directorate and is a legal anomaly. The normal legal situation is to either (a) have a holding company with subsidiaries that are limited liability companies, or (b) to have an entity – limited liability or otherwise – with internal departments or divisions.

It is equally submitted that the clumsy nature of the reorganisation with respect to the observations of the learned author will have adverse effects on the taxation of the activities of the NNPC. For instance, merging a corporate entity with an internal department may encourage under-assessment or non-assessment of the concerned corporate entities. As observed by the author, it might be that lawyers were not consulted in the exercise.

2.2 LEGISLATIONS RELATING TO PETROLEUM OPERATIONS IN NIGERIA

Various laws regulate petroleum operations in Nigeria. Incidentally, the term "petroleum operations" was not defined in the Petroleum Act, albeit it has been stated that petroleum operations means the winning or obtaining and

[80] Omorogbe Y., ibid p. 105.

transportation of petroleum or chargeable oil in Nigeria by or on behalf of a company for its own account by any drilling, mining, extracting or other like operations or process, not including refining at a refinery, in the course of a business carried on by the company engaged in such operations, and all operations incidental thereto and any sale of or any disposal of chargeable oil by or on behalf of the company.[81]

On the other hand, the English translation of the **Official Draft of the Oil & Gas Law of the Iraqi Republic** defines the term as all or any of the activities related to exploration, development, production, separation and treatment, storage, transportation and sale or delivery of petroleum at the delivery point, export point or to the agreed supply point… and includes Natural Gas treatment operations and the closure of all concluded activities.[82] In another vein, it means all activities of prospecting, exploration, exploitation and transportation of hydrocarbons, comprising the storage and processing thereof, especially, the natural gas processing but it does not comprise the refining and distribution of petroleum products.[83] The **Petroleum Law of the Socialist Republic of Vietnam,** giving a simplified definition provides that petroleum operations mean activities in exploration, field development, and production of petroleum, including services directly related to or supporting such activities.[84]

It is hereby submitted that, materially, both definitions are the same, as they defined petroleum operations restrictively to involve only activities related to

[81]**Section 2 of CAP P13 LFN 2004**.
[82] Art. 4(19).
[83] Art. 1, General Law on Petroleum Exploitation and Exploration in Sao Tome & Principe, Law No. 4/2000
[84] See Art 3, Petroleum Law (as amended and supplemented), No. 19/2000/QH10 of 9/6/2000.

upstream operations. The only discernible difference is that the Sao Tome & Principe Law specifically excludes refining and distribution of petroleum products from the ambit of what constitutes petroleum operations. The Iraqi likewise excluded it, albeit it could be implied. This is because the said Iraqi Law in its further definitions of such terms "transfer point", "supply point", "delivery point", and "transporter", limited them to only the activities connected with crude oil or natural gas operations. The Vietnamese Law definition is more direct and simpler, yet with the same meaning. However, in this Research and despite the clear but restrictive statutory meanings given to the term, petroleum operations shall widely be construed to include the downstream operations (that is refining and distribution of refined petroleum products). Thus the fiscal laws relating thereto (i.e., downstream operations) shall, with equal force, be considered.

Basically, and by no means exhaustive the laws that impinge upon petroleum operations in Nigeria include the following –

(a) Petroleum Act CAP 350 LFN 1990; CAP P10 LFN 2004 (with its subsidiary legislation that is the Petroleum (Drilling and Production) Regulations 1969

(b) Oil Terminal Dues Act CAP 338 LFN 1990; CAP O8 LFN 2004

(c) Oil in Navigable Waters Act CAP 337 LFN 1990; CAP O6 LFN 2004

(d) National Environmental Standards and Regulations Enforcement Agency (Establishment) Act, No. 25, 2007. This Act repealed the Federal Environmental Protection Agency Act CAP 131 1990; CAP F10 2004, but retained all Regulations made thereunder.

(e) Environmental Impact Assessment Decree No. 86 1992 (now CAP E12 LFN 2004)

(f) Oil Pipelines Act CAP 338 LFN 1990; CAP O7 LFN 2004

(g) Petroleum Production and Distribution (Anti-Sabotage) Act CAP 353 LFN 1990; CAP P12 LFN 2004

(h) Petroleum Equalisation Fund (Management Board, Etc.) Act CAP 352 LFN 1990; CAP P11 LFN 2004

(i) Petroleum Products Pricing Regulatory Agency (Establishment) Act No. 8 2003 (with its 2004 amendment).

(j) Finance (Miscellaneous Taxation Provisions) Decree (No. 2) No. 19 1998

(k) Companies Income Tax Act CAP 60 LFN 1990; CAP C21 LFN 2004

(l) Companies Income Tax (Amendment) Act 2007

(m) Petroleum Profits Tax Act CAP 354 LFN 1990; CAP P13 LFN 2004

(n) Deep Offshore and Inland Basin Production Sharing Contracts Decree No. 9 1999 (now CAP D3 LFN 2004). There is also Deep Offshore and Inland Basin Production Sharing Contracts (Amendment) Decree No. 26 1999

(o) Finance (Miscellaneous Taxation Provisions) Decree No. 30 1999

(p) Associated Gas Re-injection Act CAP 26 LFN 1990; CAP A25 LFN 2004 (with its subsidiary legislation, the Association Gas Re-injection (Continued Flaring of Gas) Regulations

(q) Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Decree No. 39 1990 (now CAP N87 LFN 2004). The principal Decree was amended by Nigeria LNG (Fiscal Incentives Guarantees and Assurances) (Amendment) Decree 113 1993.

(r) Allocation of Revenue (Abolition of Dichotomy in the Application of the Principle of Derivation) Act, No. 5 2004.

(s) Federal Inland Revenue Service (Establishment) Act 2007

For the purpose of this Research the above laws will be considered in the following order, that is

i. The laws in (b), (c), (d), (e) and (r) above will be considered under the topic Ownership, Environment and Community Issues in Petroleum Operations.

ii. The laws in (f), (g), (h), (i), (j), (k) and (l) relate to downstream operations and will be considered under the appropriate sections of the Research.

iii. The laws in (m), (n), and (o) which relate to upstream operations will be treated under appropriate section of the Research.

iv. The laws in (p) and (q) relate to natural gas operations and will be examined under the appropriate sections of the Research.

v. As to (s) that is a very recent law which establishes the Federal Inland Revenue Service, as the governmental organ charged with the administration of fiscal laws that relate to petroleum operations in Nigeria. Within the appropriate sections of the Research the Act will be examined.

vi. As to the law in (a), the Petroleum Act, it is the main or principal law governing petroleum operations in Nigeria. The provisions of the Act will be briefly considered here. However, since it equally touches upon other fiscal laws, the subject of this Research, which relate to petroleum operations, references to it shall be made in appropriate sections.

2.2.1 THE PETROLEUM ACT[85]

By section 1(1) the entire ownership and control of all petroleum in, under or upon any lands to which this section applies shall be vested in the State.[86] Under Section 2 three types of licences may be granted that is, oil exploration licences, oil prospecting licences and oil mining leases[87]. However, 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.[88] It is submitted that this provision is in tune with the liberalisation of the Nigerian investment climate in 1995 following the enactment of novel legislations.

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[85] See 2.3.4 “Petroleum Industry Reform” below, infra. This main law regulating the Nigerian petroleum industry has been slated for repeal under **Article 510 of the Petroleum Industry Bill 2008**.

[86] See also section 44(3) 1999 Constitution of the Federal Republic of Nigeria.

[87] Under the **Petroleum Industry Bill 2008,** these have been changed to **Petroleum Exploration Licence, Petroleum Prospecting Licence and Petroleum Mining Lease, see Article 271 of the Bill.**

[88] See section 2 CAP P10 LFN 2004.

For instance, **Foreign Exchange (Monitoring and Miscellaneous Provisions) Act NO. 17 1995 CAP F34 L.F.N. 2004; Nigerian Investment Promotion Commission Decree (NIPC) No 16 1995 CAP N117 LFN 2004; Investments and Securities Act No. 29 2007; and Companies and Allied Matters Act (CAMA) CAP C20 LFN 2004**. **Section 18 CAMA** provides that "any two or more persons may form and incorporate a company by complying with the requirements of this Act in respect of such company. Subject to **Sections 18 and 31 (Negative List sections), Section 17 NIPC Act** ordains that a non-Nigerian may invest and participate in the operation of any enterprise in Nigeria. Thus, where a non-Nigerian may not be given any of the licences obtainable under the Petroleum as an individual or sole trader, such a non-Nigerian could still obtain any of the licences by taking steps to incorporate a company in Nigeria

(a) *Oil Exploration Licence (OEL)*.[89] This licence is given or issued to explore for petroleum, and must not exceed an area of twelve thousand nine hundred and fifty kilometres.[90] The word "explore" is interpreted in relation to petroleum and means to make a preliminary search by surface geological and geophysical methods, including aerial surveys but excluding drilling below 91.44 metres.[91] This definition therefore specifies the activities which a licence holder or licensee has rights to conduct or carry out during the currency of the licence. The licence once issued expires on 31st December of the year in which it is issued, and "may not be longer in duration than one calendar year".[92]

[89] See Paras 1-3, Sch 1, CAP P10 LFN 2004.
[90] Section 2(1) of the Act and Reg 2(1) Petroleum (Drilling and Production) Regulations 1969.
[91] Section 15(1) of the Act.
[92] Omorogbe, Y., op cit. P.20.

However, it has been submitted that Oil Exploration Licences "are rarely given nowadays".[93] This is understandable because the "search" appears completed as the Federal Government "now has comprehensive seismic data on virtually all lands in Nigeria".[94] In short, to acquire such data was one of the reasons for issue of this licence. So, what is left is to "prospect" for oil within the searched areas. The OEL is said to be non-exclusive – that is it is not exclusive to the holder. In other words, several persons may be issued with licences for the same area.

(b) *Oil Prospecting Licence (OPL)*.[95] To "prospect" in relation to petroleum, means search for by all geological and geophysical methods, including drilling and seismic operations. The difference between Oil Exploration Licensee and to Oil Prospecting Licensee lies in the fact that the latter can embark on drilling and seismic operations in the search for oil. This is not available to the OEL holder. Second, it grants exclusivity of rights in respect of the area covered by the licence. A fee of US$10,000 is payable on application and a processing fee of equal amount is payable too. An applicant who wishes to withdraw his application for an OPL is liable to pay a fee of N20,000, apparently to discourage unserious and frivolous applications. Once granted, the successful applicant is expected to pay granting fee[96] within a specified time limit and upon payment of this fee, he becomes the licensee with the "exclusive right to explore and prospect for petroleum within the area of the grant".[97]

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[93] Omorogbe, Y., op cit. p. 21.
[94] Etikerentse, G., op cit., p. 63
[95] Paras 5-7, Schedule 1, CAP P10 LFN 2004.
[96] Also known as signature bonus.
[97] See generally, **Petroleum (Drilling and Production) (Amendment) Regulations, S.I. 3 of 2001.**

The grantor (normally the minister) determines the duration of the OPL, but it must never be in excess of five years for land and territorial waters areas and seven years for continental shelf and Exclusive Economic Zone areas inclusive of periods of renewals. Annual rent of US$10 per square mile or part thereof is payable by the licensee during the currency of the licence. Any assignment or subletting must be with the minister's prior written consent on payment of the prescribed application fee of N500,000.00.

(c) *Oil Mining Lease (OML)*.[98] The OML is grantable to a holder of an OPL but who has satisfied all the conditions imposed on the licence or otherwise imposed on him by this Act; and discovered oil in commercial quantities. Oil is deemed to have been discovered in commercial quantities by the holder of an oil prospecting licence if the Minister, upon evidence adduced by the licensee, is satisfied that the licensee is capable of producing at least 10,000 barrels per day of crude oil from the licensed area.

Also, while the term of an oil mining lease shall not exceed twenty years, and renewable thereafter, the lessee of an OML shall have the exclusive right within the leased area to conduct exploration and prospecting operations and to win, get, work, store, carry away, transport, export or otherwise treat petroleum discovered in or under the leased area.[99]

In terms of payments, an applicant for an OML pays US$500,000 as application fee, while withdrawal of application attracts a fee of N20,000.00. While the lease subsists, an annual rent is payable, albeit it is a deductible expense for

[98] Paras 8-11, Schedule 1, CAP P10 LFN 2004.
[99] See generally, Omorogbe, Y., op cit. pp. 22-23 on the "Rights and powers of holders of oil prospecting licences and oil mining leases over the licence(d) or leased area".

petroleum profits tax purposes. Like the OPL, the OML can be assigned to another company upon payment, by the lessee of the prescribed application fee of N500,000.00, but subject to the written approval of the minister.

Further on the Petroleum Act, the Minister has general supervisory powers over the operations of all categories of licence and lease holders.[100] Accordingly, he shall have access at all times to the areas covered by oil exploration licences, oil prospecting licences and oil mining leases, and to all refineries and installations for the purpose of inspecting the operations conducted therein and enforcing the provisions of the Act and any regulations made thereunder and the conditions of any licences or leases granted under the Act or under any corresponding law for the time being in force in Nigeria.[101] It will appear that the reason for this provision is to enable the Minister have sufficient information which he will include in his yearly report to the Federal Government on the progress of the oil industry in Nigeria.[102]

In order to exercise the powers effectively, the Minister has been granted power to arrest without warrant any person whom he finds committing, or whom he reasonably suspects of having committed, any offence under this Act or any regulations made thereunder, and shall hand over any person so arrested to a police officer with as little delay as possible.[103]

2.3 THE STRUCTURE OF PETROLEUM OPERATIONS IN NIGERIA

Before structure of petroleum operations in Nigeria is considered, it is apposite at this point to consider the question of world demand, and of course

[100] Section 8(1) CAP P10 LFN 2004
[101] Section 8(1)(c) ibid.
[102] Section 8(1)(b) ibid.
[103] Section 8(1)(d) ibid.

supply, of oil and gas, particularly in the face of U.S. determination to explore and utilize alternative sources of energy. This is because unfavourably declining world demand for oil will surely impact, negatively, on the accruable revenue to Nigeria. On the other hand, where supply is impeded in the face of surging world demand, likewise, Nigeria will be worse for it. Will a change in the US energy policy, in favour of renewable energy, impact the global demand for oil and gas, now or in the near future? What is the current position of world oil demand and supply?

It is not likely that a significant shift, as is currently being muted by the Obama administration, will have corresponding adverse impact on Nigeria as far as revenue generation is concerned. Rather what will impact adversely is a shift globally, that is the majority of industrialised countries acting in concert, in world oil and gas demand, rather than a shift by a single industrialised nation, notwithstanding that it is the world's number one economy?[104]

In fact the Obama administration has been roundly criticised as playing Russian roulette (solitaire-style) with America's quest for energy independence by rushing to replace fossil fuels with *unreliable and expensive renewable energy*[105], and sooner or later it will prove fatal. Why? The United States of America is the only major world power that refuses to develop its own energy resources. For instance, the U.S. administration has refused "to lift moratoriums on drilling for oil and natural gas on the outer continental

[104] A rhetorical question indeed. This is because the U.S. is fast losing its place of glory to upcoming economic powerhouses from the Asian extraction, for instance China.
[105] See, Ikuponisi F.S., "Status of Renewable Energy in Nigeria: Background for Energetic Solutions", An International Conference on Making Renewable Energy a Reality. Organised by **ONE SKY-Canadian Institute of Sustainable Living, Canada.** Abuja, Nigeria. November 21-27, 2004, p. 3.

shelf"[106], and is busy "force-feeding Americans a low-energy diet of renewable fuels, including notoriously unreliable and inefficient wind and solar power" in the name of combating global warming.[107]

By way of description, Renewable Energy includes solar, wind, hydro, oceanic, geothermal, biomass, and other sources of energy that are derived from "sun energy", and are thus renewed indefinitely as a course of nature. Forms of useable energy include electricity, hydrogen, fuels, thermal energy and mechanical force. Broadly speaking, Renewable Energy is derived from non-fossil and non-nuclear sources in ways that can be replenished are sustainable and have no harmful side effects. The ability of an energy source to be renewed also implies that its harvesting, conversion and use occur in a sustainable manner, i.e. avoiding negative impacts on the viability and rights of local communities and natural ecosystems.[108]

In contrast, the cash-rich China, earlier this year "embarked on a veritable shopping spree, snatching energy and mineral resources around the world"[109]. Thus, in February alone,

> Beijing cut oil deals worth $41 billion with Russia, Brazil and Venezuela. Among the most lucrative is an agreement with Moscow in which China will lend $25 billion to Russian oil giant Rosneft and oil pipeline company Transneft. In return, China will receive 300,000 barrels of crude a day for the next 20 years at about $20 a barrel. Beijing's growing appetite for energy has also taken it to the Middle East, where in March a Chinese consortium signed a $3.2 billion deal with Iran to develop an area beneath the Persian Gulf believed to hold 8 percent of the world's known natural gas reserves.[110]

[106] The U.S. Geological Survey estimated Colorado's Piceance Basin alone to hold 1.53 trillion barrels of oil.
[107] http://www.baltimoresun.news/oped/bal-op.energy.06jul06,0,6233094.story
[108] Ikuponisi, ibid.
[109] This includes Nigeria, following the takeover, in June this year, of ADDAX Petroleum by a Chinese firm in a transaction running into billions of United States Dollars.
[110] http://www.baltimoresun.news/oped/bal-op.energy.06jul06,0,6233094.story

The above factual, not hypothetical, scenario is just a tip of the iceberg as regards the condition of global energy demand as far as oil and gas is concerned. It is therefore submitted that the global balance of power is already shifting away from the United States towards China and other nations. For instance it has been stated that Russia, faced with dwindling supplies of its traditional sources of natural gas, is moving aggressively to exploit vast gas fields in the Yamal Peninsula in north-western Siberia, and has also laid claims to an area on the Arctic continental shelf, which Geologists believe contains nearly 25 percent of the world's hydrocarbon deposits. Two, there cannot be, in the future, a fall in demand for oil following the proven defects or disadvantages of renewable energy, which make it highly unattractive. This last point synchronizes with **Longwell's** assertion that the growth in oil demand took off after World War II and continued to rise as it fuelled unprecedented economic growth. On this account, he projects that world oil demand is

> expected to rise through the year 2010 (and beyond) at a rate of about 2 percent per year for oil and 3 percent per year for gas, (essentially because of) the significant benefits of hydrocarbon energy – namely, its low cost, its ease of use and its flexibility to enhance our lives in multiple applications (emphasis added).[111]

On the supply side, the story is not all that rosy. According to Longwell, the "catch is that while demand increases, existing production declines". What is the implication of these for Nigeria? One, the fears being bandied over the new U.S. energy policy and the quest for renewable energy need not be a concern at least in the immediate, because there will always be willing buyers for our goods, oil and gas. For instance, the recent deal between ADDAX Petroleum and a Chinese oil firm is a testimony to this.

[111] Longwell H.J., **The Future of the Oil and Gas Industry: Past Approaches, New Challenges,** "World Energy", vol. 5 No. 3, 2002, p. 101.

Two, Nigeria may not be able to meet the surging world demand for oil and gas, leading to a depletion of revenue. This is because the nation's production capacity continues to fall because of the renewed and fierce militancy in the region. Ours is a peculiar case. For instance, one of the major challenges that threaten world oil and gas supply is environmental fears. In fact, it is concern over potential climate change that has led to demands for greater control of energy use, which will consequently impede the ability to produce adequate amounts of energy.[112] But in Nigeria, our major concern, and in fact persistent headache, is militancy and this has successively eroded the country's production capacity. "Due to continuous attacks on oil installations, about 132 oil fields have been shut while the country is currently losing 1.9 (sic) barrel of crude oil per day. Its current production is within the region of 1.1 (sic) barrel per day of crude and thus puncturing the country's quest to realise 4 million barrel (per day) of crude oil by 2010".[113]

With fears of dwindling world demand allayed, we must now consider the structure of petroleum operations in Nigeria with a view to seeing how ready, baring militant attacks, we are to cope with surging world demand. Petroleum operations in Nigeria are classified under three broad categories. These are the upstream operations, downstream operations and natural gas operations. But the **Petroleum Industry Bill 2008** currently pending before the National Assembly and having gone through first and second readings at the Senate, the structure of the Nigerian Petroleum has been changed, to wit **Upstream Petroleum (PART III of the Bill), Midstream and Downstream Project**

[112] Here the proponents of renewable energy find support for their call for alternative sources of energy.
[113] See "**Niger Delta: Government, Oil Companies Count Pains of Militants Attacks", Business,** Sunday Trust Newspaper, vol. 3 No. 45, July 5, 2009, p.49.

Approval & Licensing (Part IV of the Bill) and Midstream Operations, Downstream Products and Special Provisions with respect to Natural Gas (Part V of the Bill). This approach is thought appropriate since in succeeding chapters each of them will be considered in greater detail, albeit with respect to the fiscal laws relating to each of them. It is sought in this section to provide a general overview of each category of operation.[114]

2.3.1 *UPSTREAM OPERATIONS*. These are those operations which involve the core activity of exploration and production of oil and gas. Other operation areas of the upstream sector include the following[115] –

1. surveying – tropical and planimetric; and sea bottom survey
2. civil works – mud pit construction, concrete works at rig sites
3. seismic data acquisition and interpretation
4. drilling and pipelining operations
5. crude oil transportation and storage

Incidentally the above operation areas within the upstream subsector constitute or represent opportunities within that subsector. Thus the concern here is how Nigerians can get involved as these opportunities are appropriated. It is important because the history of the industry showed that Nigerians have been short changed. It is against this background that the new initiative of the Federal Government, which is the development of Nigerian content[116] in the oil and gas industry becomes relevant and worthy of consideration. Several reasons have been advanced for the low level of local content in the petroleum operations.

[114] This approach is thought appropriate since in succeeding chapters each of them will be considered in greater detail, albeit with respect to the fiscal laws relating to each of them.
[115] Incidentally, or rather interestingly, these represent investment opportunities which abound in the upstream operations sector of the Nigerian petroleum industry. See http://www.nnpcgroup.com/upstream-opportunities
[116] The Acting President just assented to the Nigerian Oil I and Gas Industry Content Development Act 2010.

Some of them include the absence of basic petroleum related technology and good infrastructure; the lack of specific and comprehensive enabling legislation on local content and the failure by government officials to implement the existing legal provisions in the area; unwillingness of operators, who are mostly foreigners, to encourage and patronize local entrepreneurship; inability of indigenous businesses to raise the necessary funds from banks to increase their capability in an industry that is extremely capital intensive. Germane as the above reasons are, it is submitted that with the renewed initiative by the Government, the story will change.

The Nigerian Content is defined as the quantum of composite value added or created in the Nigerian economy by a systematic development of capacity and capabilities through the deliberate utilization of Nigerian human, material resources and services in the Nigerian oil and gas industry[117]. The above statutory definition is not good enough as it failed to recognise the need to make it a condition precedent that for utilization of such Nigerian element must be within acceptable quality, health, safety and environment standards, so that Nigerian content should not be taken as a safe harbour to harbour mediocrity in this sensitive sector. Thus a comprehensive definition is needed. Hence, the Nigerian Content is expressed as the quantum of composite value added or created in the Nigerian economy through the utilization of Nigerian human and material resources for the provision of goods and services to the petroleum industry within acceptable quality, health, safety and environment standards in order to stimulate the development of indigenous capabilities.[118]

[117] **Section 106 Nigerian Oil and Gas Industry Content Development Act 2010.**
[118] http://www.nnpcgroup.com/local-content.

It has also been stated that the objective of the local content development is to significantly increase the contribution of the expenditures in the upstream sector to the Gross Domestic Product (GDP) over a defined period of time. Therefore, the Nigerian Government is actively promoting the internalisation of inputs in the upstream sector, without compromising standards.[119]

In other words, it is a development initiative by the Government to help stimulate and develop local capacity in the Nigerian oil and gas industry. By so doing, Nigerians would be empowered to participate actively and massively in the oil and gas industry, particularly in the upstream sector. For instance, one of the short term directives by the Nigerian Content Division of the NNPC to all stakeholders in the industry is to the effect that fabrication and integration of all fixed platforms weighing up to 10,000 tons must be carried out in Nigeria; and fabrication of all piles, decks, anchors, buoys, jackets, pipe racks, bridges, flare booms and storage tanks including galvanizing works for LNG and process plants must be done in Nigeria.[120] However, this has been overtaken by events following the passage of the **Nigerian Oil and Gas Industry Content Development Act 2010.[121]** The Act among others require a minimum Nigerian content in any project to be executed in the Nigerian oil and gas industry and that minimum must be in consonance with the threshold set out in the Schedule to the Act.[122]

It would appear that operators in the upstream sector are either ready to comply willingly or be compelled or charged to comply. Thus, at the signing of

[119] http://www.nnpcgroup.com/public-relations/news-a-update/98-nnpc-chevron-construct-mini-refinery-at-escravos; also see generally, Etikerentse, g., op cit. pp. 221-233.
[120]See http://www.nnpcgroup.com/local-content
[121] See sections 4 and 69 of Nigerian Oil and Gas Industry Development Act 2010.
[122] See section 11 of the Act.

the Elf-USAN Project, the second deep water project in the country with Elf as the operator, the Federal Government charged the contractors to ensure that the work is done in Nigeria because the project is expected to provide a benchmark for the oil and gas industry in terms of local content. According to the Minister of State for Petroleum, Odein Ajumogobia (SAN), "we cannot go below this in future. We are making effort do domicile more of the enterprise. All the partners should ensure more of the work is done in the country."[123] On the other hand, the Managing Director of Addax Petroleum Limited, an upstream operator, made the following claims:

> Addax is keen to develop more indigenous participation in the more complex activities of its exploration and production operations such as conceptual and front end design of gas utilization facility, deepwater engineering, subsea engineering, specialized fabrication activities, procurement, project management, increased fabrication tonnage capacity, computerized logistics services and horizontal/bi-directional drilling, among others. Working with youths from a very early age to promote innovation and creativity whilst we develop their skills and competencies in a value adding manner is our strategy for Nigerian content development.[124]

By and large the future is bright for upstream petroleum operations in Nigeria, both in terms of revenue generation and empowerment and development of local capacities, capabilities and expertise. However, it is submitted that the Nigerian legislature should embrace this proactive and affirmative action of the Government by enacting a law targeted, more specifically, at development of the Nigerian content as far as petroleum operations are concerned.[125] This is because there are laws that touch upon local content as far as petroleum operations in Nigeria are concerned. Some of these will be examined.

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[123] http://www.allafrica.com/stories/2008050000136.html
[124] "The Nation Energy", The Nation Newspaper, Tuesday June 16, 2009, p. 33.
[125] The Acting President in April 2010 assented to the **Nigerian Oil and Gas Industry Content Development Act 2010**.

To begin, Etikerentse[126] observed that the definition of Nigerian content above involve two main areas, that is human resources development including the acquisition of technology and indigenous participation and physical local content. Human resources will include management and consultancy services.[127] Indigenous participation will include Nigerian companies, entrepreneurs, the Government through its NOC, the NNPC; while physical local content will involve utilization of Nigerian manufactured products and materials in petroleum operations in Nigeria, for instance fabrication[128].

Thus there are other laws targeted at enhancing local content as far as human resources are concerned. Some of the laws include **Petroleum Technology Development Fund Act** CAP 355 LFN 1990; CAP P15 LFN 2004, which is a fund for training of Nigerian graduates, professionals, technicians and craftsmen in the fields of engineering, geology, science, and management in the petroleum industry, **see Sections 1 and 2**; **Petroleum Training Institute Act** CAP 356 LFN 1990; CAP P16 LFN 2004, which establishes Petroleum Training Institute, Effurun for provision of courses of instruction, training and research in oil technology and to train technicians as well as other skilled personnel required in the oil industry, **see Section 2**, albeit by, executive fiat, the Institute has been scheduled for upgrade to a university; **National Office of Technology Acquisition and Protection Act** CAP 268; CAP N62 CAP LFN 2004, which establishes the National Office for Technology Acquisition and Promotion with the stated function, among others, of providing a more efficient process for the adaptation of imported technology in Nigeria and of

[126] Op cit. p. 223.
[127] See Schedule to the Nigerian Oil and Gas Industry Content Development Act 2010.
[128] See section 53 Nigerian Oil and Gas Industry Content Development Act 2010.

registering all contracts or agreements having effect in Nigeria on the date of the coming into force of this Act, and of all contracts and agreements hereafter entered into, for the transfer of foreign technology to Nigerian parties, **see section 4**[129]. On the other hand, Government through the NNPC has been leading local involvement in upstream operations.[130] By the provisions of Article 2.2.28vi Joint Operating Agreement (JOA) between NNPC and Joint venture operators, an operator shall give preference to a contractor that is organised under the laws of Nigeria to the maximum extent possible, provided there is no significant difference in price or quality between such contractor and others. In most cases, it is one of these provisos that knock out the Nigerian indigenous contractor!

As regards the fiscal laws relating to this sector (upstream) of petroleum operations in Nigeria, the Petroleum Profits Tax Act CAP 354 LFN 1990; CAP P13 LFN 2004; the Deep Offshore and Inland Basin Production Sharing Contracts Decree No. 9 1999 (now CAP D3 LFN 2004) and also Deep Offshore and Inland Basin Production Sharing Contracts (Amendment) Decree No. 26 1999; and Finance (Miscellaneous Taxation Provisions) Decree No. 18 1998 are found applicable.[131]

2.3.2 *DOWNSTREAM OPERATIONS*. This operational segment of the petroleum industry is "concerned with the post-production stages of oil and gas through the refining and processing stages, until it passes to the consumer."[132] From this definition, the following constitute the post-production stages, and thus, the activities which entail the downstream sector:

[129] Compare section 46 of the Nigerian Oil and Gas Industry Content Development Act 2010.
[130] See sections 5 and 6 of the NPP Act, CAP P13 LFN 2004.
[131] However, full discussion on, and analysis of, these laws have been deferred to Chapter Three.
[132] Omorogbe, Y., op cit., p. 107.

transportation, refining and distribution (marketing). These stages will be considered in turn. Further, the Government, for some time now, has been brooding over the idea of deregulation of the downstream sector. This will also be considered with a view to discovering the workable options and the best approach which, if adopted, will yield maximum effects.

(a) **Transportation**. The fact that petroleum is either gas or liquid necessarily means that transportation has to be an integral concern of any producer since large scale movement is required to specially designed installations, for instance depots. "In the early days, oil was carried in barrels, then in bulk containers, and later through pipelines and increasingly larger tankers". [133] Today, **barrel** has become the basic unit of measurement in the oil industry. Thus a barrel is a unit of liquid volume used in the oil industry, usually taken to be 42 U.S. gallons of petroleum, approximately 159 litres.[134] Thus it is possible for a single entity (company) to be involved in exploration, production, transportation, refining and distribution (marketing).[135] Transportation is two-fold: it can be transporting the produced oil to refineries by pipelines and oil tankers; or it can be transporting the refined product from the refineries via pipelines and oil tankers to the various storage points (depots). In Nigeria, refined products are transported by road tankers too. Due to increased import, imported refined products are distributed to storage outlets across Nigeria from the port by road tankers, otherwise known as bridging. Rail transportation plays a key role in products transportation,

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[133] Per Omorogbe Y., o. cit. p. 6.

[134] see **section 15(1) CAP P10 LFN 2004**

[135] Such a company is said to be vertically integrated. Compare this with a case where two or more companies jointly explore and produce, process (refine) and distribute in order to achieve economies of scale, otherwise known as horizontal integration.

but inept leadership has, overtime, decimated the Nigerian rail system, that today it has virtually no role to play in this all-important subsector of the petroleum industry.

It has been revealed that "petroleum products are distributed within the country through a pipeline network of 4,000 – 5,000 kilometres interconnected between the nation's four refineries and 21 depots".[136] However, movement of products from the depots to selling or dispensing points (that is filling stations, storage dumps, etc) is by road. The main legislation applicable to this segment of the downstream subsector is the **Oil Pipelines Act, CAP O7 LFN 2004 and the Oil and Gas Pipelines Regulations 1995** made pursuant to the Act.

By Section **11(2) of the Act** oil pipeline means a pipeline for the conveyance of mineral oils, natural gas and any of their derivatives or components, and also any substance (including steam and water) used or intended to be used in the production or refining or conveying of mineral oils, natural gas, and any of their derivatives or components. Further, any person may make an application to the Minister for the grant of a permit to survey the route for an oil pipeline for the transport of mineral oil, natural gas, or any product of such oil or such gas to any point of destination to which such person requires such oil, gas or product to be transported for any purpose connected with petroleum trade or operations.[137] It is only the holder of a permit to survey that is empowered to make an application to the Minister for the grant of an oil pipeline licence in respect of any oil pipeline the survey of the route for which

[136] Omorogbe y., op cit. p. 108.
[137] **Section 4(1)** of the Act.

has been completed by the applicant.[138] The application, whether for a permit to survey or for grant of licence, should normally be addressed to the Minister and delivered to the Director of the Department of Petroleum Resources. Secondly, the applicant is obliged to carry out an environmental impact assessment (EIA) study of the project. The powers of a licence holder are quite extensive.[139] Additionally, there are detailed requirements, guidelines and standards for the grant of a permit to survey a pipeline route and for the grant of a licence to construct and operate a pipeline in the Regulations, made pursuant to the Act.

The effect of the above provisions is that any person[140], whether natural or juristic, may make an application for permit to survey, and thereafter for grant of an oil pipeline licence. However, as at today, it is the network of pipelines constructed and operated by the Petroleum Products Marketing Company Limited, a subsidiary of the NNPC that is in operation. There is no private oil pipeline in Nigeria. This then is a mockery of the provision which allows for "any person" to apply for a permit and subsequently for grant oil pipeline licence. In fact, it makes nonsense of the provisions of **section 18(1)** of the Act which permits an application to be made to the Minister with respect to an oil pipeline constructed, maintained and operated in pursuance of a licence granted under this Act by any person other than the owner of the pipeline who seeks a right to have conveyed by the pipeline on his behalf any of the things mentioned in subsection (2) of section 11 of this Act which the pipeline is designed to convey. Recently, the Group Managing Director of the NNPC was

[138] **Section 7(1)** of the Act.
[139] According to Omorogbe, Y., op cit. p. 109. Such powers are generally detailed out in **Section 11(1) – (4)** of the Act.
[140] See **section 18(1) CAP I23 LFN 2004**.

quoted as stating that "the PPMC is to be unbundled as part of the reform in the downstream sector. When unbundled, it will be partly owned by the NNPC and the National Transport Logistics Company (NTLC). Further, petroleum pipeline systems and jetties loading facilities to be made available to the licenced petroleum marketing companies on an open access non-discriminatory basis as an objective of the unbundling" [141]

It is therefore submitted that there is need to overhaul the legal regime and thus encourage private participants into the scene. This could be done by either making regulations, deriving from the powers under the principal Act, which directly encourage private participants to invest in the construction, maintenance and operation of an oil pipeline, or through the enactment of a new law, which effectively puts the stamp of deregulation upon this segment of the downstream subsector.

As will be seen shortly[142], our government talks indiscreetly and, in fact, unadvisedly. For instance, it hurriedly established the Petroleum Products Pricing Regulatory Agency in 2003 with a mandate to, among others, oversee the implementation of the relevant recommendations and programmes of the Federal Government as contained in the White Paper on the report of the Special Committee on the review of Petroleum Products Supply and Distribution specified in the Second Schedule to the PPPRA Act. Yet a cursory look reveals that the Agency was rather enmeshed and occupied with the myopic object of price manipulation and tinkering as its major focus. As has been rightly observed, subject to the presence of private participants of

[141] **"Business Energy", Daily Trust Newspaper**, vol. 22, No. 10, Friday July 10, 2009, p. 34. Until that is done in practical terms, the status quo, as captured above, remains the case.
[142]. See **2.3.2(c) "Distribution",** below.

course, in several developed countries third party access is accepted and accommodated, and "the distribution networks function efficiently and the pipeline users have a choice as to which organisation they should utilize".[143]

(b) **Refining**. The laws that regulate refining in Nigeria include the **Petroleum Act[144], Hydrocarbon Oil Refineries Act[145] and Petroleum Refining Regulations.** For instance, no person shall refine any hydrocarbon oils save in a refinery and under a license.[146] Thus, any person who refines hydrocarbon oils in contravention of the provisions of section 1 of the Act shall be guilty of an offence, and shall be liable- (a) on summary conviction, to a fine of not less than four hundred naira or more than two thousand naira or to imprisonment for a term of two years, or to both; (b) on conviction on indictment, to a fine of an unlimited amount or to imprisonment for a term not exceeding five years, or to both. Additionally, any hydrocarbon oils in respect of the refining of which a person is convicted of an offence under this section shall be liable to forfeiture.[147] Additionally, no refinery shall be constructed or operated in Nigeria without a licence granted by the Minister.[148] **Section 13(2) CAP P10 LFN 2004** prescribes a paltry fine of a maximum amount of N2,000 against any person who constructs or operates a refinery in Nigeria without a licence. With this background what are the processes involved in petroleum refining?

Thus, once oil has been produced from an oil field, it is treated with chemicals and heat to remove water and solids, and the natural gas is separated. The oil

[143] Omorogbe, Y., op cit. p. 111.
[144] CAP P10 LFN 2004.
[145] CAP 170 LFN 1990; CAP H5 LFN 2004.
[146] Section 1 CAP H5 LFN 2004.
[147] section 7 CAP H5 LFN 2004.
[148] See section 3(1) and (4) CAP P10 LFN 2004

is then stored in a tank, or battery of tanks, and later transported to a refinery by truck, railroad tank car, barge, or pipeline. In fact it is at the refinery that crude oil derives its value because by itself

> Crude oil in an unrefined form has little or no direct use. Its value as a commodity is only realized when its many different hydrocarbon components are separated out, broken down or combined with other chemicals in a refinery to provide products that can be marketed. A crude oil's value… is directly related to the yield of useful products each barrel will produce as it is passed through a refinery.[149]

There are three tools used in refining[150], namely the distillation unit, thermal cracking and alkylation and catalytic cracking. Of these tools, the basic is the distillation unit. It was reported that in the United States after the Civil War of 1861-1865 more than 100 still refineries were already in operation. Today the number is better imagined. However, compare this figure with the four refineries we have in Nigeria, since discovery of oil in 1958-2009! In the meantime, the four refineries have never operated at full capacity (all the refineries have combined installed capacity of 445,000 barrels. The result is that today we are importing refined products more than many non-producing nations.

Basic Distillation Unit. The earliest refineries employ this process or tool, otherwise known as "stills" to separate the various constituents of petroleum by heating the crude oil mixture in a vessel and condensing the resultant vapours into liquid fractions. With the distillation unit, crude oil vaporizes at a temperature less than that required to boil water, but "hydrocarbons with the lowest molecular weight evaporate at the lowest temperature, successively higher temperatures are required to distil larger molecules". Initially the primary product was kerosene, despite that the first material to be distilled

[149] Omorogbe, Y., op cit., p. 9.
[150] Todd M. Doscher, "Petroleum", Microsoft Encarta, 2008.

from crude oil is the gasoline fraction, followed by naphtha, a forerunner of unfinished gasoline and which initial application was as a solvent. But little use existed for them then. The later years of the 19th century saw the development of the internal-combustion engine and this drastically created a small market for crude naphtha.

Thermal Cracking. However, the development of the automobile at the turn of the century sharply increased the demand for quality gasoline, and this finally provided a home for the petroleum fractions that were too volatile to be included in kerosene. As demand for automotive fuel rose, methods for continuous distillation of crude oil were developed. This led to the development of the thermal cracking process.

> In this process, the heavier portions of the crude oil were heated under pressure and at higher temperatures. This resulted in the large hydrocarbon molecules being split into smaller ones *that form the lighter, more valuable fractions such as gasoline, kerosene, and light industrial fuels*, so that the yield of gasoline from a barrel of crude oil was increased (emphasis added).[151]

The thermal cracking process was more advantageous than the distillation system because gasoline manufactured by the cracking process performed better in automobile engines than gasoline derived from straight distillation of crude oil. However, in terms of efficiency, the thermal process was limited because "at the high temperatures and pressures that were used, a large amount of coke[152] was deposited in the reactors", which requires the use of still higher temperatures and pressures to crack the crude oil.

Alkylation and Catalytic Cracking. In the 1930s more powerful engines were developed for aircraft. This brought about the need for an increase in the combustion characteristics of gasoline and spurred the development of lead-based

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[151] Ibid.

[152] In response, a coking process was invented in which fluids were re-circulated, enabling the process to run for a much longer time with lesser build up of coke.

fuel additives to improve engine performance – hence alkylation and catalytic cracking processes were introduced in the 1930s to increase further the gasoline yield from a barrel of crude oil. For instance,

> In the catalytic cracking process, the crude is cracked in the presence of a finely divided catalyst. This permits the refiner to produce many diverse hydrocarbons that can then be recombined by alkylation, isomerisation, polymerization and catalytic reforming to produce high antiknock engine fuels and chemicals. The production of these chemicals has given birth to the gigantic petrochemical industry which turns out alcohols, detergents, synthetic rubber, glycerine, fertilizers, sulphur, solvents, and feedstocks for manufacture of drugs, nylon, plastics, paints, polyesters, food additives, supplements, explosives, dyes, and insulating materials (emphasis added).[153]

Today, and with improved refining processes, the petroleum industry is able to meet the demands of high-performance combat and commercial aircraft and to supply increasing quantities of other transportation fuels. From the foregoing, it can be seen that crude oil is a product with many parts. Hence, once refined, irrespective of the refining process adopted, crude oil "yields three basic grouping of products which are produced when it is broken down into cuts or fractions: gas and gasoline, middle distillates, and fuel oil and residue cuts".[154]

The gas and gasoline constitute the lighter or white products. Coming from the top end of a barrel of crude oil, they provide domestic gases, aviation fuels, motor fuels and feedstocks for the petrochemical industry.[155] On the other hand, the middle distillates refer to products "the middle of a hypothetical barrel of crude such as kerosene, and light gas oil heating oil, diesel oils and waxes (and) some lubrication oils".[156] The bottom end cuts include the black

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[153] Between 1978 and 1989 refineries three refineries were constructed and established by the NNPC, and more recently a petrochemical complex in Eleme Rivers State was added to it. The refineries have a cumulatively combined installed capacity of 445,000 barrels per day. The refineries utilize the most modern process of alkylation and catalytic cracking with a unit name called the **Fluid Catalytic Cracking Unit (FCCU**.

[154] Omorogbe, Y., ibid p. 9.

[155] However, naphtha is extracted from both the light and middle range of distillate cuts.

[156] Omorogbe, Y., op cit. p. 10.

and heavy products used for power stations, industrial boilers and ship furnaces, including asphalt for roads construction, amongst others.

(d) **Distribution**.[157] **Section 4 of Petroleum Act** provides that no person shall import, store, sell or distribute any petroleum products in Nigeria without a licence granted by the Minister. There are however exemptions.[158] That is to say, the prohibition does not apply to the storage, sale or distribution of not more than 500 litres of kerosene, and such other categories of petroleum products as may be exempted by the Minister by order published in the Federal Gazette; and (b) storage of petroleum products undertaken otherwise than in connection with the importation, sale or distribution of petroleum products. The PPMC, a subsidiary of the NNPC sells products to marketers for domestic consumption. But this is as far as the NNPC can go.

This is because the body with powers to regulate the supply and distribution of petroleum products in Nigeria is the **Petroleum Products Pricing Regulatory Agency (PPPRA)**.[159] Other functions of the Agency include to establish an information and data bank through liaison with all relevant agencies to facilitate the making of informed and realistic decisions on pricing policies; to oversee the implementation of the relevant recommendations and programmes of the Federal Government as contained in the White Paper on the report of the Special Committee on the review of Petroleum Products Supply and Distribution specified in the Second Schedule; to maintain constant surveillance over all key indices relevant to pricing policy and periodically

[157] Distribution, here, includes marketing of refined petroleum products. See 1.7 "Operational Definition of Terms".
[158] Subsection 2 thereof.
[159] Established by the **Petroleum Products Pricing Regulatory Agency (PPPRA) Act, No. 8 2003 (and amended in 2004). The Agency has been slated for closure since the establishing Act is among the Acts slated for repeal under the Petroleum Industry Bill 2008, see Article 510 of the Bill.**

approve benchmark prices for all petroleum products; to prevent collusion and restrictive trade practices harmful in the sector; etc.

How are prices of petroleum products determined in Nigeria? **Section 6(1) of Petroleum Act** ordains that the Minister may by order published in the Federal Gazette fix the prices at which petroleum products or any particular class or classes thereof may be sold in Nigeria or in any particular part or parts thereof. With this clear provision of the law what is the position of the **Petroleum Products Pricing Regulatory Agency** with powers, among others, to determine the pricing policy of petroleum products and moderate volatility in petroleum products prices, while ensuring reasonable returns to operators.[160] Sadly, the Petroleum Act provision was not repealed by the PPPRA Act, so it is still an existing law.

There is therefore serious and urgent need to correct this legislative mix up. This is having regard to the provisions of **section 2 of the Petroleum Equalisation Fund Act** which states that "the Fund shall be utilized for the reimbursement of oil marketing companies for any loss sustained by them solely and exclusively as a result of the sale by them of petroleum products at uniform prices throughout the country *being prices fixed by the Minister* pursuant to *section 6(l) of the Petroleum Act*." The only inference that can be drawn from the above provisions, it is submitted, is that where the PPPRA fixes any price for sale of products throughout the country, and any oil marketing company incurs or sustains loss thereby, the PPPRA acting, on behalf of the Government of course, can refuse to reimburse such losses on the "technical reasoning" that the prices were not fixed by the Minister. It may be

[160] See section 7 PPPRA Act 2003.

rhetorically asked, what led to the unexplained fuel shortages that recently rocked the country between the months of May and June this year?

With the advent of PPPRA can we say that there is sanity as regards products distribution in the country? Hitherto, as a process in the distribution system,

> PPMC sells to petroleum product marketing companies who are to conform to laid down guidelines for steady distribution and sale at uniform prices throughout the country. Dealers are paid a commission or margin for products lifted and sold. The uniform pricing system is funded from the Petroleum Equalisation Fund. The Fund is for the reimbursement of oil marketing companies for any losses sustained as a result of the uniform pricing system. The money is apparently from net surplus revenue recoverable from an oil marketing company.[161]

The above scenario appears to be currently obtainable, save in cases where the major oil marketing companies imports the products directly into the country. In such a case they will distribute to their retail selling points or outlets. Thus, assuming, but not conceding, that major oil marketing companies now import their products directly into the country, does the PPMC still have a role to play in the distribution chain? Indubitably yes. For instance, the independent marketers may not have, individually, the financial clout to embark upon products importation. Therefore, the NNPC imports and delivers to storage facilities of PPMC which now distributes to selling points of independent markets and to NNPC retail outlets across state capitals in Nigeria. Third, the refineries have pipe network that directly connects them to PPMC facilities, so that if and when the refineries begin to operate at full installed capacity, thereby abating import needs, the major markets and independent marketers will still fall on them for their retail requirements.

[161] Omorogbe, Y., op cit., p. 114. The Fund was established pursuant to **Petroleum Equalisation Fund (Management Board, etc.) Act** CAP 352 LFN 1990; CAP P11 LFN 2004. See **sections 1, 2 and 5** of the Act. Omorogbe, Y., ibid, submitted that "the current state of this fund is unclear", that is deriving from the spate of price increases and the current pricing regime of petroleum products in the country.

From the above, it would appear that the function of the PPPRA as a regulator of the supply and distribution of petroleum products does not hold much water. One can only regulate what one can control. The state of supply, per time, of petroleum products in the country cannot be controlled by the PPPRA. Thus, if the PPPRA attempts to activate this function by directing the major marketers as to which part of the country they should direct their products to, they (the major marketers) may react, by refusing further importations. It is therefore submitted that the PPPRA as presently constituted serves little or no useful purpose as far as products distribution in the country is concerned. Rather, the PPPRA is busy flouting the very basis of its existence, confirming the fact that nothing durable can be built on a faulty foundation.

It must be recalled that the PPPRA was hurriedly established as a panic reaction to the scathing fuel scarcity in the country. However, since establishment it has not done much to improve the products supply and distribution system. In fact, the core functions of the Agency, which would have endeared it to the people if purposively pursued, appears to have been recycled to the dustbin of administrative complacency and executive inaction. For instance, the Agency's function among others includes fighting collusion and restrictive practices, yet the PPPRA on several occasions have taken sides with the marketers. The Agency fixes price regime, yet, in line with its establishing Act, it neither lays before the National Assembly the parameter and indices used in determining the pricing policy, nor does the Agency seek the approval of the National Assembly for any price regime fixed by it before its implementation. An example will suffice. Recently, when the world oil prices plummeted from over US$70 per barrel to less than US$40 per barrel

there was clamour by Nigerians for downward review of petroleum products prices, since the Agency benchmarked world oil prices in determining its pricing regime. Yet the Agency did not act.

It took direct Federal Government intervention for the price of PMS to be reduced from N70 per litre to N65 per litre. Even when this was done, the PPPRA did not see the need to wade and compel the marketers to sell at the Government-determined price of N65 per litre. Assuming the N65 per litre was the handiwork of the PPPRA, did it lay before the National Assembly the parameter for determining the new pricing policy? Did it seek the approval of the National Assembly before implementing the new prices? No, the PPPRA did none of these things. Secondly, the Agency is mandated to oversee the implementation of the White Paper on the report of the Special Committee on the review of Petroleum Products Supply and Distribution contained in Schedule 2 of its establishing Act, but this has been left unattended to since its establishment to date.

In a nutshell, petroleum products distribution in Nigeria is beset with problems. The refineries' combined installed capacity of 445,000 barrels per day can no longer support the daily needs of Nigerians (that is, even if the refineries are operating functionally at full capacity).[162] Sadly, the refineries have been left to near ruins stage due to lack of proper maintenance. In many instances, the mandatory Turn Around Maintenance (TAM) programmes of the refineries have been deferred, neglected or poorly handled. Apparently resulting from this, it has been asserted that the past several years "have been characterised by under-producing refineries that are inadequately

[162] Currently Nigeria's daily need of premium motor spirit (PMS) is said to be in millions of barrels per day.

maintained"[163] Further, our abysmal culture of neglect does not square with refinery life expectancy and revival. On this it has been revealed that refineries "usually have a lifespan of up to 20 years, but they are constantly being adapted and upgraded to remain viable and responsive to ever changing patterns of crude supply and product market demands".[164] Today petroleum products importation has become the norm, rather than the exception, even as government is not prepared to take steps that will pull the country out of the cesspool of intermittent products scarcity. Over 50 licences have been issued by the government for establishment of private refineries, yet not one has cast the Biblical stone.

2.3.3 NATURAL GAS OPERATIONS[165]. Natural gas means gas obtained in Nigeria from boreholes and wells and consisting primarily of hydrocarbons.[166] This terse statutory definition can be effectively supplemented by another simpler but clearer definition of natural gas as a colourless, highly inflammable gaseous hydrocarbon consisting primarily of methane and ethane, both of which are gaseous under atmospheric conditions [167] or pressure. It occurs in association with crude oil, and can be present as a gas cap above the oil, technically known as associated gas. Most natural gas is formed from tiny water-dwelling organisms, including algae and protozoan (known as planktons) that accumulated on the ocean floor as they died. These organisms were slowly buried and compressed under layers of sediment. Over millions of

[163] According to Omorogbe Y., op cit., p. 116.
[164] per Omorogbe, Y., op cit., p. 12
[165] Under the reformed petroleum industry, natural gas operations will now fall under midstream operations. See **Part V of the Petroleum Industry Bill 2008**.
[166] Section 2 CAP P13 LFN 2004.
[167] "Natural Gas", Encyclopaedia Britannica. Ultimate Reference Suite. Chicago: Encyclopaedia Britannica, 2009.

years, the pressure and heat generated by overlying sediments converted this organic material into natural gas.[168]

On the other hand, there are reservoirs that contain gas only and no oil. Where this is the case, the case is called non-associated gas.[169] The unique properties of natural gas make it more advantageous and attractive than, and preferable to, other species of fossil fuels. Two examples will bring out this point: one, due to its "natural gaseous state it can only be commercially transported in gaseous form via pipelines, or in liquefied form in specially constructed cryogenic tankers."[170] Two, it has been claimed for natural gas that when it burns completely, carbon dioxide and water are normally formed. The combustion of gas is relatively free of soot, carbon monoxide, and the nitrogen oxides associated with the burning of other fossil fuels. In addition, sulphur dioxide emissions, another major air pollutant, are almost non-existent.

In other words, natural gas is environmentally friendly and a preferable choice to other energy sources derivable from hydrocarbons. Also, this is a case against the proponents of renewable energy, since natural gas is in the family of fossil fuels that have continuously received barrage of attacks for being the chief culprit of global warming and harmful environment practices.

What is the natural gas situation in Nigeria? Nigeria is among the major countries that accounted for nearly 90 percent of the world's total recoverable natural gas. Other countries include Russia, the United States, Iran, Saudi Arabia, Canada, China, Turkmenistan, Norway, Mexico, the United Arab

[168] See, Whitney, G., "Fossil Fuels", Microsoft Encarta, 2008.
[169] See generally for a history of the discovery and use of natural gas, "Natural Gas", Encyclopaedia Britannica. Ultimate Reference Suite. Chicago: Encyclopaedia Britannica, 2009.
[170] According to Omorogbe, Y., op cit., p. 55,

Emirates, Qatar, Kazakstan, Venezuela, Indonesia, Kuwait, Australia, Algeria, Uzbekistan, Malaysia, The Netherlands and Ukraine. This means that exploitation of Nigeria's natural gas potentials is a commercial viability. Even before the stage is set for Nigeria to maximise the fiscal potentials of this virgin sector of the petroleum industry, there are already observed cases of near or total absence of transparency and accountability in this subsector. For instance, the House of Representatives Committee on Gas was piqued by the tardiness of the NNPC when the Corporation stated that it did not have records of natural gas produced or sold by the Nigerian Liquefied Natural Gas (NLNG), after nearly 10 years of its operation.[171] The Committee rightly alleged collusion to defraud Nigeria.

Accordingly there are extant legislations in this area that (a) encourage investment in natural gas contracts and (b) discourage wastage which leads to environmental pollution, otherwise known as gas flaring. These include, **Petroleum Act; Oil Pipelines Act; Oil and Gas Pipelines Regulations 1995; Petroleum Profits Tax Act; Companies Income Tax Act; Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Decree No. 39 1990 Act CAP N87 L.F.N. 2004 as amended by Nigeria LNG (Fiscal Incentives Guarantees and Assurances) (Amendment) Decree 113 1993; and Associated Gas Re-Injection Act CAP 26 LFN 1990; A25 LFN 2004.**[172] The laws relative to fiscal regime in this sector will be considered in greater detail in appropriate sections of this Research. For now, it suffices to state that there

[171] Nkwazema S., "NNPC: No Record of Gas Sold by NLNG", In: http://www.pppra-nigeria.org/NNPCNLNG.pdf. The statement at a public hearing on 6/5/2008 on "*a Bill to Amend the Nigeria LNG Act, CAP N87 LFN 2004*". Till date, the said Bill is said to be passed into Law!
[172] For further reading, see Adeniji, G., "The Legal Framework for Natural Gas Utilisation in Nigeria", A paper presented at The International Bar Association 2000 Conference, Held in Abuja Nigeria between 27th-28th November 2000; : http://www.pppra-nigeria.org/NNPCNLNG.pdf

exist great potentials for boosting Nigeria's revenue through massive investment in natural gas contracts.

2.3.4 PETROLEUM INDUSTRY REFORM.[173] Currently there is a Bill at the National Assembly (NASS) to revolutionize and reform the Nigerian petroleum industry. The bill, which when passed will repeal many of the laws that relate to the industry, has gone through the second reading at the Senate is called **Petroleum Industry Bill 2008.** The Bill is said to be "the most far-reaching and most comprehensive piece of legislation with over 500 provisions"[174] and covers virtually every aspect of governance and operations across the petroleum industry value chain, ranging from fundamental objectives of state policy, institutional framework, upstream and downstream operations, fiscal system and to matters of health, safety and environmental and community relations. The bill will among other things unbundle the NNPC into autonomous units. Albeit yet to be passed it has generated mixed reactions from interest groups.

On the part of the government, the Managing Director of NNPC was quoted as saying that the passage of the bill will put the industry on a strong pedestal and boosts its benefits to Nigerians as it will change the landscape of the oil and gas industry in the country. In the same vein the Minister of State for Petroleum complained that Nigeria's fiscal regime was probably too lax, hence the need for a fiscal regime that would allow the government to get a

[173] See "The Nation Energy: NNPC Chief Advocates Quick Passage of Petroleum Bill", The Nation Newspapers, Vol. 3, No. 1089, Tuesday, July 14, 2009, p. 31; "Business: Oil Giants Grumble at Nigeria's Oil Reforms", The Daily Trust Newspaper, Vol. 22, No. 12, Tuesday, July 14, 2009, p. 25.

[174] It is submitted that this does not "most far-reaching and most comprehensive". Thus, it might be arguably said that the Bill have covered fairly sufficient grounds.

significant part of the upside, since Nigeria has all along being at the bottom pile in terms of fiscal regime relative to other countries.

On the other hand, the International Oil Companies (IOCs) were of the view that the bill, if passed in its present state, will be dysfunctional to investment in the sector, essentially because many provisions in the bill "are unclear and open to multiple interpretations which would substantially increase investment risk, comparatively placing Nigeria at a disadvantage for inflow of foreign investment". Further, they warned that the new tax will decrease by half the capital investment in the sector over the next 10 years; new oil and gas production will be reduced by 50 percent; government economic rents (e.g., royalties) will decline in the long term and overall economic growth will be affected. These are the various views trailing the Bill.

However, the various views may have merit in their own right, it will be premature to comment on either position until the law is passed and assented to so that it attains the status of a law. The views canvassed are at best presumptive, pre-emptive and anticipatory. Generally, it is to be noted that issues like this bill is bound to generate the kind of controversial reactions it is receiving. One, the oil industry is still the number one contributor to the country's gross domestic product. Two, globally the oil industry hold the last card to countries who earnestly desire to walk their way to prosperity. Therefore, each side is bound to present its case in the way that best supports its inclinations, its aspirations and its expectations.

The Petroleum Bill tackles the entire petroleum industry, and is divided into 10 Parts with over 500 provisions. In **Part I** it has the **Fundamental**

Objectives, which among other provisions vests ownership of petroleum in the sovereign state of Nigeria for and on behalf of the Nigerian people. The Part has a novel provision which requires that "the management and allocation of petroleum resources and their derivatives in Nigeria shall be conducted strictly in accordance with the principles of good governance, transparency and sustainable development of Nigeria", while binding the Institutions and the National Oil Company (the successor to the NNPC) to the principles of the **Nigerian Extractive Industries Transparency Initiative Act 2007.**

Part II of the Bill establishes the Institutions that shall oversee the reformed petroleum industry. At the head to superintend the activities of other Institutions is the Minister (**see Article 9 of the Bill)** in charge of petroleum who shall have "overall supervisory functions over petroleum operations and all the Institutions of the (petroleum) industry". **Article 37** establishes the **Nigerian Petroleum Inspectorate,** the successor to the DPR, a creature of executive fiat. One of the objects for the creation of this Institution is to "ensure the efficient, safe, effective and sustainable infrastructural development of upstream petroleum operations". To achieve this object, it is vested with responsibilities, in the form of functions, under **Article 39** which include but not limited to ensuring and enforcing the compliance of all permits issued for upstream petroleum operations, setting and establishing standards relating to technical aspects of the upstream operations, including environmental standards which shall be established in collaboration with the Federal Ministry of Environment or any other agency, etc.

Other Institutions established by the Bill are **the Petroleum Products Regulatory Authority**, apparently a successor to the moribund **Petroleum Products Pricing Regulatory Agency, National Midestream Regulatory Agency, Nigerian National Petroleum Company Limited, the National Petroleum Research Centre, National Frontier Exploration Service, Petroleum Equalisation Fund and the Petroleum Technology Development Fund**, as a successor to the present PTDF.

The **Bill has** provisions relating to **Health, Safety and Environment** in Part VII. Although the Bill states that the "Regulatory Institutions shall have responsibility over all aspects of health, safety and environmental matters in respect of the petroleum industry, it is without prejudice to the overall responsibility of the Federal Ministry of Environment for the environment of Nigeria (see Article 422 of the Bill). Accordingly where, in formulating regulations relating to the petroleum industry, the Regulatory Institutions differ on issues with the Federal Ministry of Environment, there shall be a meeting involving representatives of the Ministry and the Institutions to resolve the difference, but where no agreement is reached, the directions or regulations of the Ministry of Environment shall prevail.

There is a problem with this provision. First, the Regulatory Institutions are agencies under the Ministry of Petroleum Resources. Second, within the Ministry of Environment there is equally a statutory agency (that is, the National Environmental Standards, Regulatory and Enforcement Agency, NESREA). The Bill should have provided for the Regulatory Institutions to consult and confer with NESREA and not with the Ministry of Environment.

Third, provisions of the Bill here are clear cut, so potential for conflict has been foisted on the bodies – the Regulatory Institutions on the one hand and the Ministry of Environment on the other. It is therefore submitted that the National Assembly will do a good job by tinkering with the Bill as presently constituted, otherwise role conflict as between the two are inevitable.

Part VIII of the Bill contains Fiscal Provisions. The provisions of this Part of the Bill shall be considered in detail in Chapters Three and Four of the Research. Part IX contains Repeals, Transitional and Savings Provisions. On the other hand, Part X of the Bill contains Interpretation and Citation. Particularly, the Interpretation aspect of the Bill leaves much to be desired as many interpreted words and phrases remain cloudy, ambiguous and technical to convey any meaning. And it showed that the Bill, though comprehensive, is a much hushed and hurried work.

Before now, there have been efforts by the Government to bring about reform specifically in the downstream operations. Lending his views in this direction, Dr. Braide K.M. postulated deregulation in the downstream could take one or more five scenarios or probable modes, that is "supply side deregulation" "demand side deregulation", "complete deregulation", phased deregulation, starting from the upstream sector", and retention of status quo.[175]

Among the bases for embarking upon the "supply side" mode of deregulation is the basic assumption that government would unbundle the NNPC and so abolish government monopoly of refining, pipeline operations and distribution

[175] Braide K.M., "Modes of Deregulation in the Downstream Sector of the Nigerian Petroleum Industry", in http://www.nigerdeltacongress.com/marticles/modes_of_deregulation_in_the_dow.htm.

from state-owned storage depots; and private importers would procure refined products and sell at deregulated prices, etc. The author bemoans that this mode of deregulation could be hampered because the "sorry state of the state-ran refineries, pipeline networks and depot operations may not encourage private investors to acquire them". This position, it is submitted, cannot be completely true. This is because the previous administration in its twilight hurriedly sold two of the state refineries at ridiculous prices and in a process that was shrouded in secrecy and enmeshed with indecency. This informed the reversal of the sale by the present administration.

This is against the "demand side" mode of deregulation which could be adopted by the government on the assumption that state control and monopoly on products importation would stop while private importers would have access to products reception jetties (for instance Atlas Cove in Lagos[176], Escravos, etc) and price fixing and bridging subsidies would stop. Interestingly, this mode, if adopted, will not contemporaneously lead to adequate availability of refined products because of the "lead-time to attaining improved performance and sufficient supply by existing government-owned refineries." The author predicts that with this scenario, there may now "be an upsurge in private importation of petroleum products" to complement shortfalls in product stocks. It would appear that this mode appears most attractive to the Government. For some time now, the government has been making pronouncements to the effect that it will remove subsidies from petroleum products before the end of the year.

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[176] This reception jetty was bombed the militant group, Movement for the Emancipation of the Niger Delta (MEND) on 12/7/2009. See "Theatre of Conflict Widens: MEND Bombs Atlas Cove Jetty" Daily Trust Newspaper, Vol. 22 No. 12 Tuesday, July 14, 2009, p. 1; ""Theatre of Conflict Widens: MEND Bombs Atlas Cove Jetty" Daily Trust Newspaper, Vol. 22 No. 12 Tuesday, July 14, 2009, p. 1.

Where the government adopts the mode of complete deregulation of the downstream sector it will proceed on the premise that would have to restructure all state owned refineries, pipelines and storage depots, precedent to their unbundling and acquisition by private investors. While price fixing in any guise must stop, the author hypothesized that "two separate and independent downstream policy formulation and enforcement agencies would be established by the Federal Government to monitor the sector effectively". However, it would appear that the author did not advert his mind to the existence of PPPRA as a policy formulation and enforcement agency. Secondly, the author failed to state precisely what would be the nature of the functions, and extent of the powers, of the suggested agencies.

Leaving aside the other two modes (i.e. phased deregulation and the "do nothing option" which retains the status quo hence "business unusual as usual"), the author concludes that state-owned monopolies may be dismantled completely; state interventions through the Petroleum Equalisation Fund and bridging reimbursements may cease to be; and there must be a change in pricing policy. The conclusions of the author are sound, having regard to the bandied ideals and aspirations of the Petroleum Industry Bill 2008.[177]

2.4 OWNERSHIP, ENVIRONMENT AND COMMUNITY ISSUES

This point shall be considered separately under **Ownership Issues, Environment Issues and Community Issues**. The order is random and not one of importance.

[177] See n. 74 p. 37.

2.4.1 *OWNERSHIP*. It has earlier been pointed out that the Constitution and other relevant laws vests the entire property in and control of all minerals, mineral oils and natural gas in under or upon any land in Nigeria or in, under or upon the territorial waters and the Exclusive Economic Zone of Nigeria in the Government of the Federation. In other words, ownership rights over hydrocarbon deposits in situ reside in the Nigerian state.

Ownership is a composition of rights, which someone possesses and can exercise in respect of property. These rights include the power to enjoy, and thus determine how to use, deal, destroy or part with a thing which one, usually called the owner, possesses; the right to possession meaning the right to exclude others; the right to alienate *inter vivos*; the right or power to bequeath by will; and the power to charge or mortgage as security.[178] **Blinn, K.W., et al.**, posited that there are various ownership theories in the oil and gas industry.[179] These are[180]

(a) Petroleum ownership under the United States law that principally encourages private ownership of mineral resources including petroleum. However, ownership in situ is recognized, and occurs when "the oil has been produced and reduced to possession". Deriving from this ownership paradigm, the United States Court as early as 1906 refused to "enjoin drilling by an adjacent landowner alleged to be draining oil from a reservoir under the plaintiff's land, holding that the plaintiff's remedy was self-help in drilling his own well."[181] Deepening the American legal system in this area, the Texas courts in 1915

[178] Paton, G.W., and Derham D.P., A Textbook of Jurisprudence, in Omorogbe, Y., op cit., p. 30.
[179] Blinn, K.W., et al, International Petroleum Exploration and Exploitation Contracts, Euromoney Publications, 1986, Ch. 1, In Omorogbe, Y., op cit., p. 31-34.
[180] For the purpose of this Research, only two theories will be discussed.
[181] **Barnard v. Monogahela Natural Gas Co.,** 216 Pa. 362, 65 A. 801 (1906) in Blinn, K.W. et al, n. 163 above.

"adopted another ownership concert… that oil and gas beneath the earth belonged to the person who owned the land".[182] The implication of the above is that there are today two ownership concepts in the United States: qualified ownership and absolute ownership.

Qualified ownership theory holds that the landowner does not have title to the oil and gas in situ since he can be divested by drainage without consent and without any liability being incurred by the person causing the drainage. To activate his ownership rights, the landowner must take steps to drill wells upon his land.[183] Absolute ownership, on the other hand, regards the landowner "as having title in severalty to the oil and gas in place beneath his land".[184] He loses his title to an adjacent operator the moment the "oil from his land migrates or straddles to the adjacent land and is produced from his neighbour's well". In practical terms, the two theories are similar in effect, since both theories do not vest the landowner with title to the oil and gas in situ, but only allows him the right "to sink as many wells as he desires subject to good operating practices", and to extract as much petroleum as he can.[185]

(b) The Domanial System, vests ownership rights in the state and is the most prevalent system of ownership of minerals. With the exception of the United States, virtually all countries retain sovereign ownership of minerals and enshrine them in their respective statutory documents. For instance, see, ARTICLE FIRST, The Hydrocarbons (Petroleum and Gas) Law of Afghanistan; Article 3, Petroleum Activities Law of the Republic of Angola, Law No. 10/04 of

[182] Omorogbe, Y., op cit., p. 32.
[183] According to Omorogbe, Y., ibid, "this theory obtains in states such as California and Indiana."
[184] Omorogbe Y., op cit., p. 33. The theory obtains in such states as Texas, Pennsylvania, and Arkansas.
[185] Omorogbe, Y., ibid.

12th November 2004; Article 2(1) General Law on Petroleum Operations in Sao Tome & Principe Law No. 4/2000 August 23; Article 6 Petroleum Law No. 3/2001 of 21 February of the Republic of Mozambique. In Nigeria, the Federal Government[186] exercises ownership over all minerals, mineral oils and natural gas in, under or upon –

i. The territorial waters,
ii. Continental Shelf, and
iii. The Exclusive Economic Zone of Nigeria.

The Nigerian Territorial Waters means any part of the open sea within twelve nautical miles of the coast of Nigeria (measured from low water mark) or of the seaward limits of inland waters.[187] This definition is in synchrony with Article 3 of the 1982 UN Convention on the Law of the Sea which notes that "all states have a right to establish the breadth of the territorial sea up to a limit not exceeding 12 nautical miles (22 km) from the baselines". Before now, territorial waters used to be determined by the cannon-shot rule, which transmuted to 3 mile rule, for example before 1967 Nigeria's territorial waters covered a three-mile limit before its extension to 12 nautical mile limit. This rule[188] was traceable to Bynkeershoek, a Dutch jurist, who stated that "*terrae potestas finitur ubi finitur amorum vis*", that is to say **territorial sovereignty extends as far as the power of arms goes.** Like Nigeria, other countries have adopted the 12-mile limit, for instance, the UK in the **Territorial Sea Act 1987;** and the US by virtue of **Proclamation No. 5928 in December 1988.** As regards the word **'baselines'** this refers to the width of the territorial sea

[186] see Section 44(3) Constitution of the Federal Republic of Nigeria, CAP C23 LFN 2004
[187] Section 18(1) CAP I23 LFN 2004; also see Territorial Waters Act CAP 428 LFN 1990; CAP T5 LFN 2004 (as amended by Territorial Waters (Amendment) Decree No. 1 of 1998.
[188] Etikerentse, G., op cit., p. 11.

defined from the low-water mark around the coasts of a state. Accordingly, every coastal state's sovereignty extends its territorial waters and to the airspace and seabed and subsoil but subject to the provisions of international law.[189] In other words, the territorial waters of Nigeria are an undeniable part of the territory of Nigeria with sovereign rights to exclude foreign nationals and vessels from fishing within these areas.

In Contrast, **the contiguous zone** is a zone bordering upon the territorial sea and must be specifically claimed.[190] Like the territorial waters, contiguous zones were limited to a maximum of 12 miles from the baselines. Thus, if a coastal state already claimed a territorial sea or waters of 12 miles, as in the case of Nigeria, the question of contiguous zones would no longer arise. However, see **Article 33** of the 1982 UN Convention on the Law of the Sea which prescribes that a state may claim a contiguous zone of up to 24 nautical miles from the baselines. It has been submitted that such an extension was required in order to preserve the concept, in view of the accepted 12 mile territorial waters limit.[191] Under the 1958 UN Convention on the Territorial Sea, the contiguous zone has limited purposes mainly for prevention of breaches to, or punishment of infringement of, a state's customs, fiscal, immigration, etc regulations. However, under the 1982 UN Convention on the Law of the Sea, the contiguous zone forms part of the exclusive economic zone – meaning that the character or nature of zone has taken on a dramatically new coloration. Hence, as will be seen shortly, Nigeria can validly lay claim to the petroleum within its contiguous zone complex.

[189] See Articles 1 and 2 of the UN Convention on the Territorial Sea 1958.
[190] This is unlike territorial waters that attaches automatically to the land territory of a state.
[191] Shaw, M.N., **International Law, fourth edition,** Cambridge: Cambridge University Press, 2002, p.411

It is therefore no wonder that Nigeria has statutorily exercised its sovereignty by providing that minerals etc, within the territorial waters of Nigeria are the property of the State. Hence, the ownership, control and management right of the Federal Government over the petroleum situated in the offshore areas of Nigeria was recently judicially affirmed by the Nigerian Supreme Court.[192]

The sovereign right of Nigeria over the petroleum within its territorial waters is subject to the principles of international law. Thus, it is a principle of international law that foreign vessels, as distinct from warships, are granted the right of innocent passage[193] through Nigerian territorial waters. Passage is innocent as long as a ship refrains from engaging in certain prohibited activities, including weapons testing, spying, smuggling, serious pollution, fishing, or scientific research.

The Continental Shelf Areas, means the seabed and subsoil of those submarine areas adjacent to the coast of Nigeria the surface of which lies at a depth no greater than 200 metres (or, where its natural resources are capable of exploitation, at any depth) below the surface of the sea, excluding so much of those areas as lies below the territorial waters of Nigeria.[194]

Article 76(1) of the 1982 UN Convention on the Law of the Sea, which somewhat modified the definition in the 1958 UN Convention, states that the continental shelf of a coastal state comprises the seabed and subsoil of the submarine areas that extend beyond its territorial sea throughout the natural prolongation of its land territory to the outer edge of the continental margin,

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[192] **AG Federation v. AG of Abia State & Ors (No. 2) (2002) 6 NWLR (PT. 764) 542**.

[193] Article 14 UN Convention on the Territorial Sea 1958 and Article 19(2) UN Convention on the Law of the Sea 1982.

[194] Section 15(1) Petroleum Act; see also **Section 1(1) Off-Shore Oil Revenues (Registration of Grants) CAP 336 LFN 1990; CAP O4 LFN 2004. Section 1(2) Petroleum Act,** deems the continental to be land.

or to a distance of 200 nautical miles from the baselines from which the breadth of the territorial sea is measured where the outer edge of continental margin does not extend up to that distance. This is "an arbitrary, legal and non-geographical definition".[195] Yet, academic finesse appears to adorn textual definitions of the term as can be seen from the definition of continental shelf in the following terms:

> as a geological expression referring to the ledges that project from the continental land mass into the seas and which are covered with only a relatively shallow layer of water (some 150-200 metres) and which eventually fall away into the ocean depths (some thousands of metres deep)... The vital fact about the continental shelves is that they are rich in oil and gas resources and quite often are host to extensive fishing grounds.[196]

As to the nature and extent of rights exercisable by a coastal state over its continental shelf, the International Court of Justice noted that

> The rights of the coastal state in respect of the are of continental shelf that constitutes a natural prolongation of its land territory into and under the sea exist *ipso facto* and *ab initio*, by virtue of its sovereignty over the land, and as an extension of it in an exercise of sovereign rights for the purpose of exploring the seabed and exploiting its natural resources. In short there is here an inherent right.[197]

From the definition provided by the 1982 UN Convention, where the continental margin actually extends beyond 200 miles, "geographical factors are to be taken into account in establishing the limit, which in any event shall not exceed either 350 miles from the baselines or 100 miles from the 2,500 meter isobath.[198]

Thus, taking into consideration the various definitions above and the Court's view on the inherent nature of the right attaching to continental shelf, Nigeria has inherent exclusive rights to the oil, gas, and other resources in the seabed up to 200 nautical miles (370 km) from shore or to the outer edge of the

[195] Op. cit., p. 434.
[196] Op cit., p. 432.
[197] **North Sea Continental Shelf** cases, ICJ Reports, 1969.
[198] Shaw M.N., op cit. p. 435; Article 76(4), (5), (6), (7), (8) and (9) 1982 UN Convention.

continental margin, whichever is the further, subject to an overall limit of 350 nautical miles (650 km) from the coast or 100 nautical miles (185 km) beyond the 2,500-metre isobath (a line connecting equal points of water depth).

EXCLUSIVE ECONOMIC ZONE, is an area extending from the external limits of the territorial waters of Nigeria up to a distance of 200 nautical miles from the baselines from which the breadth of the territorial waters of Nigeria is measured.[199] The exclusive economic zone is an area beyond and adjacent to the territorial sea, which should not extend beyond 200 nautical miles from the baselines from which the breadth of the territorial sea is measured.[200]

It has been canvassed that the concept of the exclusive economic zone has to some extent blurred the issue vis-à-vis the concept of continental shelf.[201] This is because Article 56 of the 1982 UN Convention, the coastal state has sovereign rights over all the natural resources of its exclusive economic zone, not excluding the seabed resources, for instance petroleum. This inevitably led to the conclusion that "states possess two sources of rights with regard to the seabed".[202] In other words, Nigeria, for instance, can claim rights over the seabed resources by asserting its sovereign rights over the exclusive economic zone or the continental shelf. The only limiting factor, as regards exclusive economic zone, is that the claim must be specifically maintained, as against the continental shelf that is inherent.[203] Also, as has been seen, the geographical reach of the continental may, permissively, extend beyond the 200 mile exclusive economic zone.

[199] **Section 1(1) Exclusive Economic Zone A**ct (as amended) CAP 116 LFN 1990; CAP E17 LFN 2004.
[200] See Articles 55 and 57 of the 1982 UN Convention.
[201] Shaw, M.N., op cit., p. 433.
[202] Ibid.
[203] Nigeria has maintained this claim specifically through the enactment of CAP E17 LFN 2004 and the 1999 Constitution of the Federal Republic of Nigeria, specifically in section 44(3) thereof.

In conclusion on matters of ownership, it has been seen that the Federal Government of Nigeria maintains firm ownership, control and management of petroleum resources through the window of legislative provisions. Nigeria's claim as regards its territorial waters, contiguous zone, continental shelf and exclusive economic zones are within the ambit of international law, whether from the perspective of treaty law or customary international law. This has fiscal implications for the country. At least, the specific claim to contiguous and exclusive economic zones has foreshadowed any likelihood of competing claims by neighbouring coastal states, except of course cases of aggression. Second, it is an assurance of increased revenue from these zones resulting from exploitation of the seabed resources within these zones.

2.4.2 *ENVIRONMENTAL ISSUES*. Environmental issues relative to the petroleum industry has to do with the potential of the industry to degrade the environment through petroleum operations. Environmental degradation is synonymous with environmental pollution, which is the addition of any substance or form of energy to the environment at a rate faster than the environment can accommodate it by dispersion, breakdown, recycling, or storage in some harmless form.[204] To what extent can environmental pollution in Nigeria be traceable to petroleum operations?

Environmental pollution in Nigeria traceable to petroleum operations is zone-sensitive. While it is agreed that generally pollution leads to depletion of the ozone layer resulting in global warming, specifically pollution in Nigeria on account of petroleum operations is, and will be, felt more within the oil producing zones of Nigeria, South-South zone, South-East zone and South-

[204] See, Omorogbe, Y., op cit., p. 127.

West zone. Within the oil-producing zones, the impact appears to be more profoundly ingrained in the Niger Delta belt of Nigeria. Therefore, instances of sources of environmental pollution in Nigeria traceable to the petroleum operations include but not limited gas flaring and oil spillage. To control pollution from petroleum operations, laws are enacted.

Hence, the legislations that relate to the activities of the petroleum industry with respect to the environment include **the Petroleum Act, Oil in Navigable Waters Act, Oil Terminal Dues Act, Associated Gas Re-Injection Act, Environmental Impact Assessment Act, Harmful Waste (Special Criminal Provisions, Etc.) Act CAP 165 LFN 1990; CAP H1 LFN 2004 and recently, National Environmental Standards and Regulations Enforcement Agency (Establishment) Act, No. 25 2007**.[205]

It would, however, appear that the NESREA Act has little application to the activities in the petroleum industry when compared to its predecessor. This is because except the functions which empower the Agency to enforce compliance with laws, guidelines, policies and standards on environmental matters; coordinate and liaise with stake holders, within and outside Nigeria, on matters of environmental standards, regulation and enforcement; enforce compliance with policies, standards, legislation and guidelines on water quality, environmental health and sanitation, including pollution abatement,[206] all other functions of the Agency carefully excluded the oil and gas industry. For instance, it is the function of the Agency to enforce environmental control

[205] Hereafter called the **NESREA Act**. **Section 36 of the Act** repealed the Federal Environmental Protection Agency Act, CAP F10 LFN 2004. However, by **section 35 of the Act** all Regulations and Guidelines and other rules aimed at controlling pollution and protecting the environment made under the repealed Act.

[206] See **section 7(a), (b), (c), (d), (e), (f),(i) and (m)** of the NESREA Act.

measures through registration, licensing and permitting systems *other than in the oil and gas sector*; and to conduct environmental audit and establish data bank on regulatory and enforcement mechanisms of environmental standards *other than in the oil and gas sector*.[207]

In the exercise of the powers conferred upon it by the Act, the Agency shall have power among others to conduct public investigations on pollution and the degradation of natural resources, *except investigations on oil spillage;* and to submit for the approval of the Minister, proposals for the evolution; review of existing guidelines, regulations and standards on environment *other than in the oil and gas sector;* do such other things *other than in the oil and gas* sector as are necessary for the efficient performance of the functions of the Agency.[208]

The implication of the foregoing is that the NESREA has clearly reduced role to play in matters relating environmental issues in the Nigerian oil and gas industry. One wonders the rationale for the inclusion of a representative of the Oil Exploratory and Production Companies in Nigeria in the composition of the Council of the Agency,[209] while the Department of Petroleum Resources, the NNPC or the Ministry of Petroleum Resources has no representative on the Council!

One of the areas, and such areas are hard to come by under the Act, where the NESREA can extend its tentacles to the oil and gas sector will be where it collaborates with other relevant agencies and with the approval of the

[207] See **Section 7(g), (h), (j), (k), and (l)** of the NESREA Act.
[208] See **section 8(g), (k), (l), (m), (n), and (s) of the NESREA** Act.
[209] See section 3(1)(c)(viii) of the Act. It might be that this provision was smuggled into the Act. In any case their representation comes to nothing, since the Agency does not have full regulatory oversight over the oil and gas industry.

Minister "to establish programmes for setting standards and regulations for the prevention, reduction and elimination of pollution and other forms of environmental degradation in the nation's air, land, oceans, seas and other water bodies and for restoration and enhancement of the nation's environment and natural resources".[210] There is a problem with this provision. Why must ministerial approval be sought before the Agency can collaborate with other relevant agencies, not Ministries? It is therefore submitted that if the Agency must effectively collaborate with other relevant Agencies[211] it must have unrestricted and unfettered power to do so, by being extricated from the apron strings of ministerial approval.

In the final analysis, it is not surprising that the NESREA has little significance to play when it comes to environmental matters relating the petroleum industry. This is because the Department of Petroleum Resources in the Federal Ministry of Petroleum Resources is the apex regulator of the oil industry, and thus has overriding power to supervise and monitor the industry in environmental matters. Albeit, sadly, there is no law that directly empower the DPR to undertake these functions.[212]

However, the wisdom of the legislature in distancing NESREA from the activities in the oil and gas sector is an attempt to avert the potential for problems of jurisdiction that may arise between NESREA and DPR. This is against the legislative blunder that included a representative of the oil exploration and production companies in Nigeria in the composition of the

[210] See section 8(o) of the Act.
[211] For instance, **National Emergency Agency, the Department of Petroleum Resources, National Agency for Foods, Drugs and Administration Control, Standards Organisation of Nigeria**, etc.
[212] See n. 67, p. 30 above.

Council of NESREA, which amounts to nothing but a nuisance. In comparison, under the predecessor of NESREA, Federal Environmental Protection Agency, had "overall responsibility for the Nigerian environment and thus the industry", but this led to problems of jurisdiction between FEPA and DPR[213]. The effect was that the oil companies had to comply with two sets of regulations from different agencies. This logjam has been taken care of in the NESREA Act. The NESREA and DPR can now horizontally cooperate and collaborate for the good of the Nigerian environment; however the requirement of the Minister's approval in the case of NESREA is a minus to this noble ideal.

2.4.3 *COMMUNITY ISSUES*. Nigeria's oil is mainly produced from the Niger Delta belt, 80 percent of which are located in Delta, Rivers and Bayelsa States, with a production capacity of over 75 percent of the nation's petroleum. According to **Omorogbe, Y.,** the oil communities within the Niger Delta are "those located in the actual areas of exploration and production", and for them the main legal issues to contend with are threefold, that is to say, "the right to development, rights over natural resources and rights for injuries suffered as a result of oil industry activities".[214] These rights appear to have been relegated to the background, judging from the grim observation of the learned author that

> for some years the oil communities have been quite militant in demanding their rights.[215] It is important to acknowledge years of neglect and apathy on the part of the federal and state governments, which are partially responsible for an abysmal level of poverty and underdevelopment that is incomprehensible to those from other parts of Nigeria.[216]

[213] Omorogbe, Y., op cit., p. 141,
[214] Op cit., p. 144.
[215] Judging from the time the work of Omorogbe Y., was published, militancy was non-existent compared to the tale of woes, of vandalisms, destructions and sabotages going on at the Niger Delta, in spite of the presence of the JTF.
[216] Op cit., p. 143.

The explanation of the author that the oil communities remain underdeveloped "because of their relative inaccessibility and higher costs of development projects (for natural reasons such as the type of soil, higher technology, distance, etc), is not tenable. This is because it is ethically, morally, socially, economically and politically wrong to muzzle the mouth of the ox that threshes the corn, on the simple reason that it is inexpedient and inconvenient. And no one can deny that the people have inalienable right to development as enshrined in the **1986 UN Declaration of the Right to Development and the African Charter on Human and People's Right.**[217] Sadly, we are now paying the price of this administrative failure and leadership misadventure in Nigeria.

Thus, the Niger Delta region today has transformed into a theatre of war, between the JTF and MEND, the two principal actors. MEND alleged that on 12/5/2009,

> the Nigerian armed forces launched an unprovoked attack on two major MEND camps in Delta State hoping to overwhelm them with the element of surprise. Unfortunately for the raiders we were waiting for them. A bloody battle is on-going and two gunboats belonging to the army have already been sunk by mines and several casualties on the side of the army.[218]

On their part, the Director of Defence Information (DDI) of the Nigerian Army issued a statement counter-alleging that on 13/5/2009, members of the JTF, Operations Restore Hope, on routine escort duties around Chanomi Creek were ambushed by a militant group leading to the unfortunate and painful loss of some military personnel.

The above claim and counter claim by both MEND and the military signalled the commencement of full scale military conflict between the MEND and the

[217]. The African Charter has been domesticated in Nigeria and is now **African Charter on Human and Peoples' Rights (Ratification and Enforcement) Act** CAP 10 LFN 1990; CAP A 9 LFN 2004, having force of law in Nigeria.

[218] "Niger Delta: What Happens to Fiscal Federalism?" Sunday Magazine, Sunday Champion Newspaper, June 21, 2009, p. 15.

Nigerian Army represented by the JTF. In one of its attacks precisely on 15/5/2009, which the JTF said were to flush out criminals from the creeks,

> air, water and land assaults were launched on Okerenkoko, Oporoza, Kurutie, and Kunukunuma communities in Gbaramatu Kingdom of Delta State. The attacks were launched… when the Oporoza community in Gbaramatu Kingdom was in a festive mood. The Ameseikumo festival in Oporoza has been halted and so many people were killed today when the JTF struck with helicopters, gunboat, jet bombers and warship, cried Chief Godspower Gbenekama, who as in Oporoza for the ceremony.[219]

The bombardment of the communities by the JTF was described as indiscriminate as many civilians were killed. Dangerously for the Nigerian military, if it can be shown that the strike was actually indiscriminate, and thus contrary to the Law of War, then it could place the men of the army involved in the operation in a tight corner, since they could be exposed to prosecution by the International Criminal Court.[220] However, on its side the MEND has consistently and continuously unleashed destruction upon strategic oil installations in the country.

Who gains and who loses from the above unfortunate incidents? Of course, the Nigerian State, without doubt, is the biggest loser. Thus, it is reported that "following the disruption of production and lack of exploration of new oil fields in the Niger Delta because of militant attacks, Nigeria's oil production level fell by four percent", which consequently led to a sharp fall in the country's oil reserves from 34 billion barrels to 32.7 million barrels.[221] This represents a huge loss in revenue to the government. This represents a potential lull in infrastructural development in the country. And it represents a

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[219] The Sunday Magazine, op cit., p. 16.

[220] See **Articles 7(1) and 8(1) of the Rome Statute of International Criminal** Court; see also, Brandon B. and Max du Plessis (Eds)., **The Prosecution of International Criminal Crimes: A Practical Guide to Prosecuting ICC Crimes in Commonwealth States,** London: Commonwealth Secretariat, 2005, pp. 35-72.

[221] "Nigeria's Oil Output Dips by 35m Barrels", The Nation Energy, The Nation Newspaper, 16/6/2009, p. 31.

dysfunction to inflow of foreign direct investment, including foreign portfolio investment, into the country.

In order to restore peace and order to the region, the Federal Government recently proclaimed amnesty to all the Niger Delta militants. To confirm its seriousness in this regard, the Federal Government entered *nolle prosequi* in respect of the criminal trial of the leader of MEND, Henry Okah, who accepted the offer and was thereafter released. However, the question remains, is that the solution to the crisis? It is not likely. This is because the strike on Atlas Cove in Lagos was carried out the day the leader of MEND was released by Government. In fact, MEND in a statement showed a dogged determination to proceed with the militancy when it said that "we want to assure our people and well wishers that we will not sell our birthright for a bowl of porridge[222] because we are not committed to anyone but the people of Niger Delta".[223] In fact, one of the commanders of MEND was reported as saying that "the release of Okah would not stop the movement from pursuing its dual gambits of dialogue and sabotage".[224]

Another dimension is brewing up to the conflict in the Niger Delta, and if not checked will diametrically alter the stakes in the region, with grave fiscal consequences for the country. It has to do with the recent decision by the National Boundary Commission and the Revenue Mobilization, Allocation and Fiscal Commission to return 75 oil wells from Cross River State to Akwa Ibom State. This decision has elicited frayed nerves and inflammatory statements from the States parties affected by the decision. While it is outside the ambit

[222] Apparently a veiled but satirical reference to the Government's proclamation of Amnesty.
[223] "Militants Blow Up Key Fuel Jetty in Lagos", The Nation Newspaper, vol. 3 No. 1089, July 14, 2009, p. 2.
[224] "MEND Vows to Continue Strikes", Daily Trust Newspaper, vol. 22, No. 12, July 14, 2009, p. 5.

of this Research to look into the merits of the decision, the position of Akwa Ibom State is worth appreciating. It defended the decision of the governmental agencies on the strength of Supreme Court decision[225] which declared that following the loss to Cameroun of the Bakassi Peninsula, the territory of Nigeria lost included the estuarine territory of Cross River State. This loss consequently hemmed in Cross River State so that it is now a non-littoral State of Nigeria. It is hereby submitted that the Federal Government should not fold its hands and watch the unfolding drama degenerate to the level of lawlessness we are currently witnessing in the region. It should intervene and thus save the nation from further losses in revenue, which is direly needed in these times of global economic downturn.

Happily, the Federal Government for the first time has acted auspiciously in resolving the Niger Delta crisis. Thus, with its ingenious offer of Amnesty[226] to the militants, restiveness was abated as almost all the militants, led by their leaders, embraced the offer. The amnesty is meant to engage the militant youths in more constructive and legally productive activities in the Nigerian economy. It involves a conscious programme of the government to adopt a feasible and balancing developmental programme for the Niger Delta. The noble ideals of the amnesty programme are sure to succeed if backed by sincerity and honesty of implementation. And it is submitted that there will be no excuse for failure as the government has left itself with no room for such failure. This is because with the creation of Federal Ministry of Niger Delta and the continued existence of the Niger Delta Development Commission, an agency of the Federal Government, all chances and excuses for failure have

[225] A.G. Cross River State v. A.G. Federation and Anor (2005) 15 NWLR (PT. 947) 71.
[226] The Amnesty took effect 1 August 2009.

been foreclosed. It is hoped that the government will not slack, relent or weary in this task.

2.5 CONTRACTUAL ARRANGEMENTS IN PETROLEUM OPERATIONS

Earlier, we had seen the power of the minister to issue certain licences under the powers derived from the Petroleum Act in that behalf.[227] These licences are contractual but do not fundamentally touch upon fiscal regime in the petroleum industry. However, what will be considered under this head are the legal arrangements which exist between the various operators and the Nigerian Government through the NNPC for the exploration and production of crude oil in Nigeria. These arrangements directly touch upon the fiscal regime, and their full import and impact will be considered in subsequent Chapters of the Research.

The various types of legal arrangements for upstream petroleum operations in Nigeria are "the concession", "the joint venture, represented by the Joint Operating Agreement (JOA)[228]", "the production sharing contract (PSC)", "the service contract", and arrangements involving indigenous companies and marginal fields, known as sole-risk. However, under the PIB, **Article 272(2**) specifically provided for three model contracts which the National Oil Company or any other oil company is empowered to enter, namely **Production Sharing Contracts; Risk Service Contracts,** which provides for reimbursement of "the oil company contractor for costs where a discovery is made and shall be entitled to payment in cash or from crude oil or natural gas produced from the contract areas"; and "**any contract being a variation of production sharing contracts or risk service contracts, which for the time being is an internationally acceptable mode of awarding contracts for exploration and production of oil or natural gas, as the case may be."** For

[227] See pp. 37-41 above.
[228] The Joint Venture is construed synonymously with Joint Operating Agreement (JOA) in this Research.

the purpose of this Research only JOA, PSC and arrangements involving indigenous companies will be discussed. This is because they relate more directly with the fiscal regime as is currently obtainable in petroleum operations in Nigeria.

(a) **Joint Venture (JV).** The JV emerged following government's acquisition of participation interests in the concessions[229] held by oil companies. Under the JV the relationship of the parties were as defined by (i) the participating agreement, and (ii) the operating agreement, collectively hereafter called the JOA. The JOA is supplemented by a third agreement called the Memorandum of Understanding (MOU).

The JOA operates as a partnership form of agreement between the joint venture partners, the NNPC and the oil companies. In other words, the JOA spells out the extent of participatory interest of each of the partners and equally designates one of the partners as the operator of the venture, normally the oil company. The JOA, as the main document governing the partnership, governs the relationship between the parties in such issues as budget approval and supervision, crude oil lifting and sale in proportion to equity, and funding obligations of each of the partners. The supplemental document, the MOU, spells out the formula for allocating revenue from the venture as between the partners, covering such areas as taxes, royalties and industry margin. Under the JOA, the tax rate is as stipulated under the Petroleum Profits Tax Act CAP P13 LFN 2004, that is 85% of chargeable profit.

[229] Actually, the concession is OML as stated under the Petroleum Act.

However, it has been indicated that there are constraints that plagued the JOA, and these include poor funding, due mainly to the imbalance in the financial capacity of the different joint venture partners, allegations by non-operators of the venture of gold plating of operating costs leading to mutual distrust between the parties, and the peculiar challenge of meeting the incessant demands by oil producing communities[230] and currently the spate of militancy leading to attacks on oil installations and facilities. Undoubtedly, the Joint Venture is becoming unattractive.

(b) **Production Sharing Contract (PSC).** Several factors led to the introduction of this form of contractual arrangement into the Nigerian oil and gas industry. They range from fiscal to operational factors. One of such factors is the emergence of offshore oil and gas operations and granting deep water acreages to the oil producing companies. Other factors attributable to a shift from JOA to PSC have been revealed to include the following:

> Complexity of operations in the offshore terrain (which makes regulation under a JOA more difficult); the dwindling resources of the country (which makes funding under the JOAs precarious and susceptible to oscillations in government generated revenue); it is a convenient funding arrangement that will enable the country to achieve her objective of increasing oil and gas reserves without necessarily committing additional financial resources thereto (emphasis added).[231]

The PSC is said to originate in Indonesia in 1966, modelled after share cropping in farming. Under this, where the owner of land grants a farmer the rights to grow crops on his land and share the proceeds with the farmer on agreed proportions after the harvest. Obviously, the farmer with the technical knowhow in agriculture does not have the land where he can apply his skill and expertise and thereby add value to himself. The land is the alternative

[230]Ameh M.O., "The Nigerian Oil and Gas Industry: from Joint Ventures to Production Sharing Contracts", In: http://www.hollerafrica.com/showarticle.php?catId=2&artId=85

[231] Ameh, M.O., op cit.

forgone; the opportunity cost is the share of the proceeds of his sweat, the price he has to pay for not owning the land. So, under the PSC, the contractor, usually an oil company bears the entire cost and risk of exploration activities and reaps the rewards after, if there is, a commercial find.

Once there is commercial recovery, the contractor recovers its costs fully, called cost oil. Allowances are made for tax oil and royalty oil. The remainder, called **profit oil** is shared in agreed proportions between the company the government, represented by the NNPC. The peculiar feature of the PSC is that there is provision for ring fencing of the oil wells covered by the arrangement. This simply means that taxation is on the basis of production per contract area, so that the loss from one oil block cannot be carried into the profit from another as off-set. Hence, there is potential of total loss exploration costs by the company.

The PSC is new and covers mostly acreages in the shallow and deep offshore areas and the inland basins. The NNPC in furtherance of the PSC signs specific contracts with each individual company. The authority of the NNPC for entering into the first generation of PSCs appears to be derived from **section 22 of the Petroleum Profits Tax Act CAP P13 LFN 2004** which provides that a crude oil producing company which executed a Production Sharing Contract with the Nigerian National Petroleum Corporation in 1993 shall, throughout the duration of the Production Sharing Contract, be entitled to claim an investment tax credit (ITC) allowance of 50 percent as an offset against tax in accordance with the provision of the Production Sharing Contract.

This was however followed by the **Deep Offshore and Inland Basin Production Share Contracts Act CAP D3 LFN 2004 (as amended).** As will be seen in this Research, the tax incentives under the PSC are juicer than that under the JV. For instance, the Act provides for flat tax rate of 50% on petroleum profits by PSC operators, while setting different royalty regimes, "depending on the water depth in which the operation is carried out, ranging from 12 percent for water depths of 200-500 meters, to 0% for water depths in excess of 1000 meters;" and all operations in the inland basins[232] attracts a flat royalty of 10%. Another incentive is investment tax credits and allowances available to investors at the rate of 50% of the value of such investment. The concomitant effects of these provisions on the revenue of the government will be considered in the next Chapter of this Research.

The PSC has been hailed as possessing great advantages as far as the management of petroleum operations in Nigeria are concerned. Thus, there is no financial burden on the part of the government, even after a commercial find; the payment to the contractor is in oil equivalent; there is room for "leveraging on the technical knowhow and experience of the companies in such operations", in other words it adds a boost to the local content initiative of the Nigerian government, amongst others. However, the major drawback of the PSC is that in the event of an unsuccessful commercial find, the operator/contractor bears the risk of loss. There is thus ring-fencing of the oil wells, because taxation is on the basis of production per contract area. This drawback could seriously affect the choice of acreages which an operator is ready to accept for exploration. This, in turn, will discourage the ideal of the

[232] The Act declares that Inland basins means any of the following Basins, namely, Anambra, Benin, Benue, Chad, Gongola, Sokoto and such other basins as may be determined, from time to time, by the Minister.

government as regards the inland basin areas, to wit to stimulate interest in exploring for petroleum in these areas. Therefore, it is submitted, a further incentive may be needed so that in the event of unsuccessful find, the operator is not left to bear the cost alone.

(c) **Sole-Risk Arrangements.** This is an arrangement which is primarily targeted at indigenous operators as licence holders. This is so because they "are mostly shut" from Joint Venture and PSC arrangements.[233] Historically the policy was introduced in 1989 during the military regime of General Ibrahim Babangida. In fact, "the concessions granted thereunder were those that were relatively easy to exploit. The criteria for grant include (a) the ownership of the company must truly reside in Nigerians who must not be agents or fronts for foreigners; the grantee may have foreign technical partners who must not own more than 40 percent interest in the OPL or OML, and they (the foreign companies) must not be any of the existing major companies engaged in petroleum exploration and production business in Nigeria; (c) the managing director of the grantee company must be a Nigerian, but where he or she is expatriate, he or she must be an employee of the grantee company; (d) the government reserves the right of participation in the venture; and (e) the profits of the grantee company are taxed under the Petroleum Profits Tax Act, including the application of **section 19(2) PPTA**.[234] In other words, the sole-risk arrangement is a deliberate governmental policy aimed at boosting Nigerian indigenous participation in the upstream sector of the Nigerian

[233] Arogundade, J.A., **Nigerian Income Tax & Its International Dimension**, Ibadan: Spectrum Books Ltd, 2005 p. 249.
[234] It is submitted that this amounts to reviving the repealed Nigerian Enterprises Promotion Decree by other means.

petroleum industry.[235] However, the nature of licence grantable under this policy is the OPL, which in any case could transform to OML.

Here the government is a party to the grantee of the concessions. Lofty as the ideals of the policy are, it was discontinued in 1999 by the previous civilian administration. The reason for discontinuation was that the process of awarding the grants lacked transparency and there was no level playing field for all Nigerians. It is submitted that it was easy to discontinue by mere executive because it was a policy not backed by any law.

Another form of contractual arrangement, which appears to be a replacement of the discretionary awards of OPL to indigenous companies, is the grant of marginal fields.[236] A marginal field has been defined as

> an oil field in a concession that is held by a major oil company not containing a significant discovery or due to certain reasons (for example economics, low API gravity, high viscosity, the field having high and low oil reserves, etc) the field is left un-produced for a considerable length of time.[237]

In other words it is a nonproducing field whose economics is not considered sufficiently robust using conventional development methods under the prevailing fiscal regime.[238] As much as possible a distinction between the sole-risk and Joint Venture will be brought out in the subsequent Chapter.

CHAPTER THREE

FISCAL LAWS RELATING TO UPSTREAM OPERATIONS

3.0 INTRODUCTION

[235] Greater boost has been given to Nigerians with the enactment of the Nigerian Oil and Gas Industry Content Development Act 2010.

[236] See, **Marginal Fields Operations (Fiscal Regime) Regulations S.I. No. 8 2006, made pursuant to section 9 PPTA.**

[237] Etikerentse, op cit. p. 97.

[238] Omorogbe, op cit., p. 170.

The fundamental law regulating the fiscal aspects of upstream petroleum operations in Nigeria is the Petroleum Profits Tax Act (PPTA) CAP P13 LFN 2004 and copiously supplemented by Deep Offshore and Inland Basin Production Sharing Contracts Act CAP D3 LFN 2004, hereafter PSC Act, and the Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Act CAP N87 LFN 2004, hereafter the “Incentives Act”.[239] Subject to its passage into law, the aforementioned laws, save the Incentives Act and section 16 subsections (1) and (2) of the PSC Act, will be repealed by the Nigerian Hydrocarbon Tax under the Petroleum Industry Bill 2008 currently before the National Assembly for enactment into law.[240]

Under this Chapter, the above enactments will be considered with a view to pointing out the extent of their efficacy, and identifying pitfalls, loopholes, and lacunas, if any, which the taxpayer is bound to exploit under the technical nicety, or euphemism, of tax planning, or more commonly mundane phrase of tax avoidance.[241]

3.1 PETROLEUM PROFITS TAX ACT (PPTA)

Promulgated in 1959, but retroactively effective from 1/1/1958, this principal law that regulate upstream petroleum operations in Nigeria has witnessed many amendments. In the course of this section, the amendments shall be reckoned with.

3.1.1 Overview of the PPTA

The PPTA comprises 11 Parts with four Schedules. Part I, otherwise Preliminary, is made up of two sections. True to its name, it has the

[239] So called by Onamson, F.O., “Energy: A Bird’s Eye View on Fiscal Provisions of Petroleum Industry Bill”, The Nation Newspaper, Vol. 3, No. 1138, Tuesday September 1, 2009, p. 31 and Vol. 4, No. 1145, Tuesday September 8, 2009 p. 31

[240] See pages 51-57 above.

[241] Tax Avoidance and Tax Evasion are treated under Tax Planning in Chapter Five – Administration and Enforcement of Fiscal Laws Relating to Petroleum Operations In Nigeria, infra.

interpretation section, where such technical words as 'adjusted profit', 'assessable tax' 'chargeable tax', 'non-productive rents', profits, etc, were defined. Part II, made up of five sections (i.e. sections 3 to 7) is the Administration part. Thus by virtue of section 3(1)(a) the due administration of this Act and the tax shall be under the care and management of the Board[242] which may do all such acts as may be deemed necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in a manner to be prescribed by the Minister. The Service is defined to mean the Federal Inland Revenue Service established and constituted in accordance with section 1 of the CITA.

However, following the enactment of Federal Inland Revenue Service (Establishment) Act, 2007, and the repeal of Part I of Companies Income Tax Act, the Federal Board of Inland Revenue (FBIR) ceased to exist. Thus the Federal Inland Revenue Service (FIRS) was subrogated into the position of the defunct FBIR as far as the administration of the PPTA is concerned. Accordingly, by virtue of **sections 2, 8, 25 and 68 and FIRST SCHEDULE** of the Act, the FIRS is vested with the administration of the PPTA.[243]

Further, Part III comprising 13 sections (to wit, sections 8 to 20) provides for imposition of tax and ascertainment of chargeable profits. For instance, section 11 provides incentives to encourage companies to engage in utilisation of associated gas. Provided the company meets the conditions specified under subsection 2, any investment by the company required to separate crude oil and gas from the reservoir into usable products shall be considered as part of

[242] Now, the Service by virtue of Federal Inland Service Act 2007, see Chapter Five, infra.
[243] The extent to which the FIRS discharges this supreme role of administering the fiscal laws relating to petroleum operations in Nigeria is the subject of a separate Chapter in this Research, see Chapter FIVE, infra.

the oil field development; capital investment on facilities equipment to deliver associated gas in usable form at utilization or designated custody transfer points shall be treated for tax purposes, as part of the capital investment for oil development; and capital allowances, operating expenses and basis of tax assessment shall be subject to the provisions of this Act and the tax incentives under the revised memorandum of understanding.[244]

Part IV, made up of three sections (sections 21 to 23) deals with ascertainment of assessable tax and of chargeable tax; while Part V comprising six sections (see sections 24 to 29) is on persons chargeable. Thus under section 24 it is an offence for an individual or individuals in a partnership to engage in petroleum operations. However, companies can engage in petroleum operations by way of partnership arrangements.[245] On this Etikerentse observes that the reason for the prohibition may be because "the petroleum profits tax rate is higher than the rate for personal income tax".[246] With respect, the learned author missed the point. The reason for the prohibition may be informed by the huge capital outlay required for any person wishing to venture into upstream petroleum operations; and secondly, it makes for a neater arrangement for companies to be so required since registered companies are by law required to comply with certain standards in the preparation of their statement of accounts, a position not obtainable in the case of an individual or partnership.[247]

[244] See page 103, infra.
[245] Also, Article 455 PIB 2008 creates it as an offence where individuals in partnership engage in upstream petroleum operations with a view to sharing profits arising from those operations.
[246] Op cit. p. 247.
[247] See PART XI, Financial Statements and Audit, of PART A, CAMA.

However, the wider implication of this provision can be seen when viewed against the requirements of the law[248] which ordains that a non-Nigerian may participate in the operation of any enterprises in Nigeria, in so far as such enterprises do not fall within the 'negative list'. The negative list is those sectors of investment prohibited to both non-Nigerians and Nigerians, and incidentally petroleum enterprises, hitherto included, are conspicuously missing. Hence, it is permitted sector of investment. An enterprise is said to mean industry, project, undertaking or business to which the NIPC Act applies.[249] A business can be entered into by an individual, whether Nigerian or non-Nigerian and the law permits this. In fact the individual may do so in partnership with others provided the number does not exceed 20.[250]

In other words, it is a negation of the spirit behind the NIPC Act to now prohibit individuals from engaging in upstream petroleum operations. It is therefore submitted that the law ought to be amended to take care of such individuals who can muster the capacity and clout to venture into this sector of investment. Although it may be argued that the spirit of the NIPC Act was not in any way affected, since what the PPTA requires is that participation must take a certain form, through a registered company form instead of partnership or sole trader. In any case, to address the observed fears of government, provision could be made requiring such individuals to comply with set standards in the preparation of their statement of accounts and audit.

[248] See Sections 17 and 18 Nigerian Investment Promotion Commission Act, CAP N117 LFN 2004.
[249] Section 31 CAP N117 2004.
[250] See section 19 and Part B CAMA.

Corollary to the above, no tax shall be charged under the provisions of the **Personal Income Tax Act**[251] or any other Act in respect of any income or dividends paid out of any profits which are taken into account, under the provisions of this Act, in the calculation of the amount of any chargeable profits upon which tax is charged, assessed and paid under the provisions of this Act.[252]. Justification for providing for this exemption is hard to find. After all dividends received by an individual from other corporate undertakings are subject to tax. It is the individual who is being taxed of income from a source inside or outside Nigeria, not the company that paid the petroleum profits tax: hence it cannot be said that it would amount to double taxation. Here the company bears the burden or incidence of the tax.

In the final analysis, the provision is a legislative ploy to make the rich richer, and the poor poorer and to subject the Nigerian people to cringe of economic domination by its foreign predators. However, and as regards taxation of dividend income from other companies other than companies subject to PPTA, it must be borne in mind that "income tax is only paid on the profits of a company once and where those profits are distributed to shareholders, whether corporate or individual, by way of dividends the burden of income tax is ultimately passed on to the shareholders".[253]

In addition, Part VI accounts and particulars is made up of five sections (sections 30 to 34), as against Part VII (consisting of six sections of sections 35 to 40) which deals with assessments. Part VIII made up of three sections

[251]See sections 3, 12, 13 and 15 Personal Income Tax Act 1990.
[252] Section 60 PPTA.
[253] Per M.T. Abdulrazaq, Nigerian Revenue Law, 2005, Lagos: Malthouse Press Limited, p.134. See Prof. M.T. Abdulrazaq, "Legal Mechanisms for Corporate Tax Relief", **Juriscope**, Vol. 1, 2nd Edition, Port Harcourt, 2002, p. 127.

(sections 41 to 43) is on appeals. Under this Part, appeal against any assessment by the FBIR (now, and hereafter to be called, FIRS) shall lie to the Body of Appeal Commissioners, whose sitting shall be held in camera.[254] This provision, and indeed a substantial aspect of this Part, is inconsistent with the FIRS Act. For instance, the FIRS Act created in section 59 the Tax Appeal Tribunal, with power to settle disputes arising from the operations of the laws under the First Schedule, of which the PPTA is inclusive. Under the Fifth Schedule paragraph 15(5), all appeals before the tax appeal commissioners shall be held in public.

Happily section 68 thereof resolved these inconsistencies to the effect that if the provisions of any other law, in this case the PPTA or any other law, are inconsistent with the provisions of the FIRS Act, the provisions of the latter shall prevail and the provisions of the former shall *pro tanto* be void.

Moreover, Part IX comprising seven sections (sections 44-50) is on collections, recovery and repayment of tax. On the other hand, Part X deals with offences and penalties and is constituted by nine sections (that is, sections 51 to 59). Part XI with four sections (sections 60 to 63) contains miscellany, for instance matters of double taxation arrangements, non-applicability of income tax laws on sums distributed as dividends after account has been taken of such sums in the petroleum profits tax payment, etc. Capping it, the Act contains four schedules. First schedule contains powers or duties to be performed or exercised by the Service alone; second schedule contains table of capital allowances that touch on sections 10, 17, 20 and 30; third schedule provides for the due dates for payment of PPT. In fact it is only paragraph 3 of the

[254] See section 41(6) PPTA.

schedule, to wit that the tax due date for each year shall be payable in monthly instalments. Schedule four defines certain terms connected with petroleum profits tax calculations for natural gas operations.

3.1.2 Scope of the PPTA

In this research, we defined petroleum operations widely to include downstream petroleum operations.[255] However, this is not the case as far as the scope of the PPTA is concerned. Thus, under the PPTA petroleum operations do not include downstream activities in the Nigerian petroleum industry. In other words the restrictive definition of the term applies.[256] The Court had held that the mere act of transporting a cargo of petroleum from Nigeria to a consignee who did not himself win or obtain it by drilling, etc is not sufficient to constitute 'petroleum operations' for the purposes of the PPTA. It has equally been rightly observed that the operations of servicing companies (normally engaged in geophysical, seismic or drilling) though incidental to petroleum operations cannot constitute petroleum operations since such companies would not have won, drilled or obtained chargeable oil for its own account. Petroleum refining companies are excluded too. All excluded companies are subject to CITA.

However, under the Hydrocarbon Tax of the Petroleum Industry Bill currently before the National Assembly, companies subject to hydrocarbon tax (i.e. PPT) shall now simultaneously be subject to CITA, a position which is not obtainable under the PPTA. However, until the Bill passes into law, the current position is that companies taxable under the PPTA are not subject to tax under the CITA.

[255] See page 24 above.
[256] See section 2 PPTA; pp. 23-24 above.

But where such companies engage, as shall be seen, in activities that do not fall under petroleum operations, the profits derived therefrom will be subject to tax under CITA.[257] Thus, only companies engaged in petroleum operations as defined by the Act that are subject to PPT.

It is important however to note, and bear in mind, that the PPTA, albeit the principal taxing statute for (upstream) petroleum operations in Nigeria, is not the only taxing Act impinging upon upstream petroleum operations. Thus, for petroleum tax purposes there are three main fiscal regimes, namely the Joint Venture Contracts (JVCs); the Production Sharing Contracts (PSCs)[258]; and the Sole Risk (Independent Operators).[259] According to the author, "the PPTA still provides the framework for the computation of the PPT but what goes into the computation is dictated by the terms of (the distinct agreements between the NNPC and the operator or concessionaire) which modify the application of the provisions of the PPTA".[260] A fourth regime may be added with respect to Natural gas operations, and this is largely dictated by the Incentives Act.[261] Thus, whatever taxing regime is applicable, the point remains that the scope of the PPTA is limited to companies engaged in petroleum operations as defined by the Act and adumbrated by the Courts.

3.1.3 Basis of Assessment under the PPTA

Section 2 of the PPTA defined "accounting period" in relation to a company engaged in petroleum operations, to mean (a) a period of one year commencing on 1 January and ending on 31 December of the same year; or (b)

[257] **Shell-BP Petroleum Development Company of Nigerian Ltd v. Federal Board of Internal Revenue** (supra).
[258] Discussed infra, see. 3.2, at p. 109.
[259] Op cit., p. 226
[260] Ibid, p. 226
[261] Discussed infra, see 3.3 at p. 117.

any shorter period commencing on the day the company first makes a sale or bulk disposal of chargeable oil under a programme of continuous production and sales, domestic, export or both, and ending on 31 December of the same year; or (c) any period of less than a year being a period commencing on 1 January of any year and ending on the date in the same year when the company ceases to be engaged in petroleum operations.

The implication of the above provision is that all companies coming within the purview of the Act have their accounting year end as 31st December. In other words, no company has the right to choose its own accounting date. For example, LIGHT CRUDE PETROLEUM LTD (LCP) was registered on 1st March 2008. It got an OPL on 1st July 2008 and discovered oil on 25th December 2008. The Company commenced production and exportation of the oil in commercial quantity on 1st April 2009. By the provisions above, LCP is deemed to have commenced business in petroleum operations on 1st April 2009. The Accounting Year will be the period 1st April 2009 to 31st December 2009 and the Assessment Year will be 2009.

A rider to the provision relating to accounting period is that in the event of any dispute with respect to the date of the first sale of chargeable oil above or with respect to the date on which the company ceases to be engaged in petroleum operations, the Minister of Petroleum Resources shall determine the same and no appeal shall lie therefrom. This provision is understandable since the Minister through the Department of Petroleum Resources (DPR) oversees all activities relating to upstream petroleum operations. Thus, no commercial

discovery of oil will have been made without the notice and certification of the DPR and the date of such discovery duly recorded.

3.1.4 Ascertaining Profits and Tax Computations under the PPTA

Per section 8 of the PPTA[262], the charging section, there shall be levied upon the profits of each accounting period of any company engaged in petroleum operations during that period, a tax to be charged, assessed and payable in accordance with the provisions of this Act. Arogundade illuminates on this section that what is taxable is "the profits" as defined by section 9; the person taxable is "any company" and not a "group of companies"; the company being levied must be participating in the petroleum operations as defined by section in section 2 of the Act; and the tax payable must be charged, assessed and payable in line with the Act, particularly sections 30 and 35 of the Act. While it is agreed that a "group of companies" is not taxable, especially under a holding a company, it must be noted that group of companies engaged in partnership, in joint adventure or in concert under any scheme or arrangement are taxable[263]. It is apt to make this distinction to clear the fog of sweeping generalisation over the submission of the author.

Additionally, it is apposite to state that where a company engaged in petroleum operations is engaged in the transportation of chargeable oil by ocean going oil-tankers operated by or on behalf of the company from Nigeria to another territory then such adjustments shall be made in computing an adjusted profit or a loss as shall have the effect of excluding therefrom any

[262] See Article 444 of the PIB 2008.
[263] See section 24(2) PPTA.

profit or loss attributable to such transportation.[264] This is a case where a company engaged in petroleum operations as defined by section 2 can be charged taxed under the CITA, as against under the PPTA, for any profits from the oil transportation business of the company.[265] This is a balanced position of the law since transportation qua transportation has nothing to do with winning and obtaining oil; charge under PPTA would work injustice since a higher rate of tax will be used; even where the company transports its own oil, it is a deductible expense; and being a different undertaking it cannot be said that the company is subject to double taxation.[266]

Proceeding from the above discussion, **profits**, in relation to any accounting period under the PPTA, is defined as the aggregate of the proceeds of sale of all chargeable oil sold by the company in that period; the value of all chargeable oil disposed of by the company in that period; and all income of the company of that period incidental to and arising from any one or more of its petroleum operations.[267]

i. *Adjusted Profits*. The adjusted profit of an accounting period shall be the profits of that period after deduction of (a) expenses allowed by subsection (1) of section 10 PPTA and (b) the profits or loss arising from transportation of the crude by ocean-going tankers, whether or not operated by the company; and (c) other non-petroleum profit.[268] The

[264] Section 14 PPTA.
[265] See I.A. Ayua, The Nigerian Tax Law, Ibadan: Spectrum Law Publishing, Rep. 1999, p. 197.
[266] The issue of double taxation is treated in Chapter Five.
[267] Section 9(1) PPTA.
[268] See Sections 9(3); 10(1); and 14 PPTA. See also, L. Soyode & S.O. Kajola**, Taxation Principles and Practice in Nigeria**, 1st Edition, Ibadan: Silicon Publishing Company, 2006, p.557.

expenses allowed under section 10 must be those "wholly, exclusively and necessarily incurred"[269] for the purpose of the petroleum operations.

They include rent, royalties, repairs, bad debts, tangible drilling costs, costs of exploration and drilling of the first two appraisal wells in a specific field, etc. Allowable deductions are to be found in Art. 445 of the PIB 2008, and includes similar, but not all, deductions as in section 10 PPTA. For instance, a novel allowable deduction is introduced which allows deductions from tax donations to university or other tertiary or research institutions provided such does not exceed 2% of chargeable profits of the company. Different percentage obtains under CITA, that is to say either 15% of total profits or 25% of tax payable, whichever is the higher. [270]

Arogundade argues that "one area of apparent contradiction is the allowance of interest on inter-company loans".[271] This is because according to section 10(1)(g) PPTA all sums incurred by way of interest on any inter-company loans obtained under terms prevailing in the open market, that is the London Inter-Bank Offer Rate, by companies that engage in crude oil production operations in the Nigerian oil industry are allowed.

On the other hand, section 13(2) contains provisions for disallowable deductions and they include but not limited to any disbursements or expenses not being money wholly and exclusively laid out or expended, or any liability not being a liability wholly or exclusively incurred, for the

[269] On the meaning of these words, the Court in **Gulf Oil Company (Nig) Ltd v. FBIR (1985) FHCLR 1,** stated that the "wholly", means "entirely, exclusively"; "exclusively" means "substantially or even solely"; and "necessarily", means "appropriately or inevitably". The Court went on to hold that the three conditions must be present simultaneously as one is not alternate to the other.

[270]See section 7 Companies Income Tax (Amendment) Act 2007, discussed in Chapter Four, infra.

[271] It would appear that this concern was taken care of in the Nigerian Hydrocarbon Tax under the Petroleum Industry Bill 2008, as it is not included in Article 445 as allowable deductions.

purpose of those operations; any capital withdrawn or any sum employed or intended to be employed as capital; any capital employed in improvements as distinct from repairs; any sum recoverable under an insurance or contract of indemnity; rent of or cost of repairs to any premises or part of premises not incurred for the purposes of those operations; any amounts incurred in respect of any income tax, profits tax or other similar tax whether charged within Nigeria or elsewhere; the depreciation of any premises, buildings, structures, works of a permanent nature, plant, machinery or fixtures. These items are not disallowed in vacuum. For example, depreciation is not allowed because under section 20 PPTA are provided capital allowances. Secondly, depreciation of assets is determined by the internal policy of any company, so that depreciation rates differ from company to company: hence, capital allowances as granted offers level playing field for all companies[272].

Further, PPTA provides that, notwithstanding this provision allowing deduction of interest on inter-company loans, in computing the adjusted profit of any company of any accounting period no deduction shall be allowed in respect of sums incurred by way of interest during that period upon any borrowed money where such money was borrowed from a second company if during that period either company has an interest in the other company; or both have interests in another company either directly or through other companies; or both are subsidiaries of another company.

Now a company shall be deemed to be a subsidiary of another company if and so long as an interest in it is held by that other company either directly

[272] See Art. 446 of the PIB 2008 for equivalent, but not necessarily similar, provisions.

or through any other company or companies; an interest means a beneficial interest in issued share capital (by whatever name called); and the Board shall disregard any such last-mentioned interest which in their opinion is insignificant or remote, or where in their opinion that interest arises from a normal market investment and the companies concerned have no other dealings between each other.

From the above, it is submitted that the author diametrically muddled up his views here. What is envisaged, and indeed intended by the Act, are inter-company loan relationships, as against intra-company loan relationships. Intra-company relationships exist where both companies have a connection between each other, with or without any loan relationship. In holding this view, the author's grouse is with the word 'any' used in section 10(1). To this, the simple answer is that the Act limited its application when it used the exclusionary word,' notwithstanding' in section 13(2) thereof.[273] Although section 13(2) refers to section 10(1)(b) dealing on royalties and not interests, it is submitted that this could not have been the intendment of the Act. In other words this could be the result of codification errors or printer's devil.

Rightly, Arogundade contends that the mischief targeted by section 13(2) is thin capitalisation.[274] Thus, by disallowing interest on loans between connected companies, the Act has removed the problem of disguise of equity as loans to gain advantage.[275] The author argues circularly that section 10(1)(g) would re-introduce the thin capitalisation problem. With

[273] See also, Section 13(3) PPTA.
[274] Op cit., p. 256
[275] Under Petroleum Industry Bill 2008 inter-company loans are outlawed completely: see

respect, this is not the case. One, the interest must have been obtained under open market transaction; and two, where the FIRS is of the view that such loan transaction was sham, artificial or fictitious, albeit the interest purports to be based on the open market, it will disregard it.

Further, section 11 of the Act provides for incentives for companies involved in gas utilization projects, both associated and non-associated.[276] Accordingly investments, for instance, required to separate crude oil and gas from the reservoir into usable products shall be considered as part of the oil field development and thus tax deductible. It is submitted that despite this provision, gas utilization projects remain low, for example companies continue to flare out gas. One wonders therefore the rationale for its continued retention. Apparently, this must have informed its removal from the Petroleum Industry Bill 2008.

On the other hand, in order to ascertain the adjusted profits of any accounting period of a company involved in petroleum operations, there are non-deductible items (or disallowable expenses) provided by the Act.[277] They include any disbursements or expenses not been money wholly and exclusively laid out or expended, or any liability not being a liability wholly or exclusively incurred, for the purpose of those operations; any capital withdrawn or any sum employed or intended to be employed as capital; any capital employed in improvements as distinct from repairs; any sum recoverable under an insurance or contract of indemnity; rent of or cost of repairs to any premises or part of premises

[276] This was an amendment to the PPTA by the Finance (Miscellaneous Taxation Provisions) Act 1998 No. 18 and Finance (Miscellaneous Taxation Provisions) Act 1999 No. 30.
[277] See section 13 PPTA.

not incurred for the purposes of those operations; etc. It is important to note that though contributions to an insurance fund, interest paid on loans, bad debts, etc. are deductible expenses, the sums thereafter received from these sources by way of refunds, releases, etc by the company must be reported as income for relevant accounting period.[278]

ii. *Assessable Profits*. After arriving at the adjusted profits as discussed above, the next thing is to discover the assessable profits for the accounting period. Assessable profit of an accounting period is the adjusted profit of that period after any deduction allowed by section 16 of the PPTA.[279] In other words it is the adjusted profit minus previous year losses. A specie of loss allowable as deductible from adjusted profit for the purpose of arriving at the assessable profit is a case concerning reconstituted company.[280]

*S*ubject to certain succeeding provisos, the amount of any loss incurred during any accounting period by the foreign company, being a loss which has not been allowed against any assessable profits of any accounting period of that foreign company, shall be deemed to be a loss incurred by the Reconstituted Company in its trade or business during its first accounting period so that the amount of that loss shall be deducted from the adjusted profits of the Reconstituted Company.[281] Etikerentse insists with an air of reiteration that the situation envisaged in this provision has ceased to exist, hence "its import does not have practical application any

[278] See sections 10(2) and 9(1)(c) PPTA.
[279] Section 9(4) PPTA.
[280] See section 18 PPTA.
[281] See section 18(2)(d) PPTA.

longer".[282] This is true because the era of protectionism is gone; the environment of indigenisation, expropriation and nationalisation has given way to economic liberalism and uncensored and unbridled capitalism.[283] In terms, this provision has no practical relevance or efficacy to serve.

But compare the PPTA with the PIB 2008, which provides that the assessable profits of any company for any accounting period shall be the amount of the adjusted profit of that period after the deduction of (a) the amount of any loss incurred by that company during any previous accounting period; and (b) in a case to which Art 450 (relating to trade or business transferred under the CAMA) applies, the amount of any loss deemed to be a loss incurred by that company in its trade or business during its first accounting period. The amount of the deduction will be made from the adjusted profit of the company.[284]

iii. *Chargeable Profits.* This is defined as assessable profit minus deductions provided in section 20 of the PPTA.[285] It has been submitted that such deductions (in section 20) relate to expenditures on items in the nature of capital and are allowed to be claimed under the provisions of the Second Schedule to the PPTA.[286] By the provisions of section 20(4) of the PPTA there is a limit as to the maximum amount that may be deducted in any accounting period.

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[282] Op cit., p. 256.

[283] See for instance sections 17, 18 and 31 of NIPC Act; and sections 3(2), 13, 15 of Foreign Exchange (Miscellaneous Provisions) Act (FEMP), CAP F34 LFN 2004. For instance, **section 15(4) of FEMP Act** which guarantees unconditional transferability of funds in freely convertible currency with respect to dividends or profits (net of taxes).

[284] See Art 448 of the PIB 2008.

[285] See section 9(5) PPTA.

[286] Etikerentse, op cit., p. 257. The details of such qualifying capital expenditures are contained in Second Schedule and include plant, machinery and fixtures, pipelines and storage tanks, drilling expenditure and construction of buildings, structures or works of a permanent nature.

Accordingly, the subsection provides that it is the LESSER of the aggregate amount of all the allowances permissible under the Second Schedule for the accounting period or a sum equal to 85% of the assessable profits of the accounting period less 170% of the total amount of the deductions allowed as petroleum investment allowances computed under the Second Schedule for that period. The reason for this limitation on deductible qualifying expenditure is to ensure that the amount of any tax chargeable on the company for that period shall be not less than fifteen per cent of the tax which would be chargeable on the company for that period if no deduction were to be made under this section for that period.[287] It is important to note that all qualifying capital expenditure attracts the following rates of annual capital allowances:

TABLE 3.1

Year	Annual Rate (%)
First year	20% per annum
Second year	20% per annum
Third year	20% per annum
Fourth year	20% per annum
Fifth year	19% per annum
Sixth year and after	19% annum

On the other hand, **TABLE 3.2** below depicts the petroleum investment allowances deductible in any accounting year:

[287] See section 20(3) PPTA.

Qualifying capital expenditure in respect of	Annual Rate (%)
On shore operations	5
Operations in territorial waters and continental shelf areas up to and including 100 metres of water depth	10
Operations in territorial waters and continental shelf areas in water depth between 100 metres and 200 metres	15
Operations in territorial waters and continental shelf areas beyond 200 metres of water depth.	20

Hypothetically, and to bring out more clearly, the point under discussion, an illustration is vital. Assuming the assessable profit of LCP Ltd for 2008 is $5m. Capital allowances claimed amounted to $3.2m and $1.4m as investment allowance. To arrive at the chargeable profit, we have to deduct $3,200,000 and $1,400,000 from $5,000,000, leaving a balance of $400,000 as chargeable profits. The assessable tax would the 85% of chargeable profits (i.e. $400,000), which is $340,000. We now have to find out if the tax meets the 15% threshold. Thus, tax as a proportion of assessable profits (i.e. $340,000 divided by $5,000,000 multiplied by 100) would yield 6.5%. As can be seen, 6.5% is less than the minimum tax of 15%.

The company has a duty to pay at least 15% tax so it must revert to subsection 4 of section 20. The application of the subsection is represented in the **TABLE 3.3** below:

Assessable Profits (A)		5,000,000
85% of Assessable Profits	4,250,000	
Aggregate (TOTAL) of all the allowances (3,200,000 plus 1,400,000).	4,600,000	

170% of investment allowance of 1,400,000.	2,380,000	
Now, 85% of assessable profits minus 170% of investment allowances would be 4,250,000-2,380,000= 1,870,000 (this amount is the allowable deduction).	1,870,000	
Allowable Deduction (B)		1,870,000
Chargeable Profits (A minus B)		3,130,000
Capital Allowances (carried forward to next accounting period) 4,600,000-1,870,000=2,730,000.	2,730,000	
TAX PAYABLE AT 85% of Chargeable Profits (i.e. 85% of 3,130,000).		2,660,500

ANALYSES:

(a) Section 20(5) allows for capital allowances not fully deducted within any accounting period to be carried forward to the next or future accounting period.

(b) From the above table, the company can only deduct $1,870,000, being the value of 85% of assessable profits less 140% of investment allowance.

(c) The sum of $2,730,000 can be carried forward to next accounting period and deducted accordingly.

The minimum tax of 15% has fiscal implications. Thus, it is submitted that the policy behind this is to ensure that either way the government of is assured of realizing its legitimate financial expectations in order to carry out and execute its programmes, to wit provision of security, infrastructure, education, agriculture amongst others. If it were not so, virtually all the companies taxable under the Act would hide under section 20 capital expenditure deductions to avoid payment of tax, and even where they succeed in paying the amount remitted to the government coffers will be nauseating to sensibilities.

Conversely, Art 452 of the PIB 2008 states that the chargeable profits of any company of any accounting period shall be the amount of the assessable profits of that period after the deduction of any amount to be allowed. The deductions to be made from the chargeable profits are (a) the aggregate amount of all allowances due to the company under the Ninth Schedule on capital allowances[288]; (b) general production allowance of $40 per barrel up to a cumulative maximum of 10 million barrels per PML for onshore; up to a cumulative of 20 million barrels per PML for offshore to a water depth of 200 meters; and up to a cumulative maximum of 40 million barrels per PML for offshore deeper than 200 meters. [289] The wisdom behind these generally profuse allowances is to encourage specifically the production from new small oil fields. On the flip side, there is also a provision for allowance to encourage development and production of new natural gas fields.[290]

Like the PPTA, where there insufficient or no assessable profits, the PIB allows for carry-over of capital allowances for any accounting period to the next accounting period. The PIB has an interesting provision to the effect that cost categories under Art 446(q), (r), (t), (u), (v), (w), (x), (z), (aa), and (ab) which are not deductible would also not qualify for capital allowance. [291] Also, costs incurred prior to the establishment of an upstream company in Nigeria are disallowed.[292] The meaning is that the company is barred from reflecting this item of expenditure as an item of capital allowance. This is an interesting provision, and illuminates further the angst of the IOCs against the PIB.

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[288] See Art 452(2) of the PIB 2008.
[289] See Art. 453(1) of the PIB 2008.
[290] See Art. 453(2) of the PIB 2008.
[291] Art. 452(4) PIB 2008.
[292] Art. 446(v) PIB 2008.

iv. *Assessable Tax*. Section 21 of the PPTA ordains that it is the tax for any accounting period of a company shall be an amount equal to 85% of its chargeable profits of that period. However, where a company has not yet commenced to make a sale or bulk disposal of chargeable oil under a programme of continuous production and sales as at 1 April 1977, its assessable tax for any accounting period during which it has not fully amortised all pre-production capitalised expenditure due to it less the amount to be retained in the book shall be 65.75% of the chargeable profits for that period.[293] It is important to note that the tax rates have risen to the present rates progressively over the years. Also, the 65.75% is mostly applicable to sole-risk operators, who may not have been able to produce a single barrel since securing OPL and OML, while a larger majority of those who have commenced production may not be able to meet the commercial quantity threshold of at least 10,000 barrels per day. Arogundade posited the reasons for this state of affairs, namely –

> The industry is capital intensive and has a high risk factor as oil may not be discovered at all or in commercial quantity. Where oil is not discovered, there is no income against which to write off the pre-production expenses. The marginal fields allocated to many of them have high operating costs. What is required in the circumstance is equity rather than debt finance and not many are able to raise such capital. As small players in the field, they cannot enjoy the economy of scale but rather have to pay high prices for spares and equipment and for services such as storage and transportation. The government has not provided incentives to mitigate the costs and risks (emphasis added).[294]

While the assessable tax is the rate of tax fixed by the PPTA as already captured above, there are circumstances in which the Minister of Finance is empowered by the PPTA to make rules for the ascertainment of assessable and chargeable tax.[295] These are with respect to companies that have in petroleum operations either in partnership, in a joint adventure or in concert under any scheme or arrangement.

[293] That is, such a company has not qualified for treatment under paragraph 6 (4) of the Second Schedule to the PPTA.
[294] Arogundade, Op cit. p. 250.
[295] See section 24(2) of the PPTA.

Plagued by the problems identified above, sole-risk operators are found in this category because they must necessarily go into some arrangements with foreign technical partners in order to meet the capital requirements for productive petroleum operations.

The power granted to the Minister to modify the provisions of the PPTA is for the purpose of making rules for the sharing of tax burden, not profit benefits, between the companies that have entered into the arrangement. Accordingly, the Minister may (a) provide for the apportionment of any profits, outgoings, expenses, liabilities, deductions, qualifying expenditure and the tax chargeable upon each company, or (b) may provide for the computation of any tax as if the partnership, joint adventure, scheme or arrangement were carried on by one company and apportion that tax between the companies concerned or (c) may accept some other basis of ascertaining the tax chargeable upon each of the companies which may be put forward by those companies and such rules may contain provisions which have regard to any circumstances whereby such operations are partly carried on for any companies by an operating company whose expenses are reimbursed by those companies.[296]

One needs not fish for the rationale behind this provision. For instance, it has been noted earlier that sole-risk operators are plagued by dearth of resources needed to support capital intensive petroleum operations. Thus they enter into agreements with foreign technical partners. Within these agreements, the foreign technical partners freely insert clauses that would ensure the recovery of their investments but which simultaneously create abuses to the tax system, consequently resulting in income shifting from Nigeria to the country of origin of

[296] See section 24(3) of the PPTA.

participating technical partners.[297] With the powers vested on him by the PPTA, the Minister attempts to strike a balance and thus ensure that assessable tax is charged and paid by every company involved in petroleum operations.

At this juncture, it must be pointed out that the assessable tax rates have risen over the years. The **Table 3.4** below traces how the applicable tax rate under the PPTA has progressively risen over the years:

S/N	YEAR	TAX RATE (%)	OBSERVATION
01	1/1/1958-20/3/1971	50	As noted above, there is at present dual or multiple tax rate regimes. For instance, by s. 21(2) a company that has not begun sales or bulk disposal of chargeable oil is liable to 65.75%. Also by virtue of s. 22 any crude oil producing company that have executed a production sharing contract with NNPC is entitled to ITC at the rate of 50% of chargeable profits for the duration of the PSC. The implication of this will be explored later.
02	21/3/1971-30/11/1974	55	
03	1/10/1974-30/11/1974	60.78	
04	1/12/1974-31/3/1975	65.75	
05	1/4/1975-TILL DATE	85 or 65.75 or 50%	

Adapted from: Nigerian Petroleum Law, 2004

To cap it, the PIB 2008 provides in Art. 454 that the assessable tax for any accounting period of a company under its purview shall be a percentage of the chargeable profit of that period as follows:

(a) For onshore and shallow offshore to a water depth of 200 meters, 50%;

(b) For frontier acreages and deep offshore for a water depth beyond 200 meters, 30%.

[297] Arogundade, ibid.

The implication of the introduction of tax rate bands under the PIB means that one company can simultaneously undertake upstream operations in both geographical zones – that is on onshore and shallow offshore up to a water depth of 200 and on frontier acreages. Where this is the case, the PIB provides that such a company shall file separate tax returns for each zone. This provision is instructive. For example, Art. 437 of the PIB 2008 ordains that royalty rates shall not only be based on production but also on geographical areas or zones. Thus, the royalty rate for onshore areas shall be 5% for the part of the production up to and including 5000 barrels per day, 12.5% for the part of the production over 5000 barrels per day up to and including 10,000 barrels per day and 25% for the part of the production over 10,000 barrels per day. Similarly graduated differential rates are provided for offshore areas.[298] The lower rate of assessable tax in respect of frontier acreages is understandable.[299] However it has been submitted that the 30% without more will not encourage investments in that area in the quantum and magnitude envisaged and desired by the government.

In other words, the government needs to do more, in the area of incentives if it is serious about encouraging activities in the frontier acreages.[300] Further, it would mean that a company engaged in both zones would end up paying assessable tax rate of 80% since it is expected to file two separate returns on which the FIRS will make its assessment. However, the minimum tax payable by any upstream company is 30%, while the

[298] See Art 437(2) of the PIB 2008.

[299] Frontier acreage is defined as any or all licences or leases located in the Anambra, Benue Trough, Bida, Chad, Dahomey and Sokoto Basins of Nigeria (known under CAP D3 LFN 2004 as inland basins)

[300] Per Onamson, F.O., "Energy: A Bird's Eye View on Fiscal Provisions of Petroleum Industry Bill", The Nation Newspaper, Vol. 3, No. 1138, Tuesday September 1, 2009, p. 31 and Vol. 4, No. 1145, Tuesday September 8, 2009 p. 31

maximum is 80%, 5% lower than the rate obtainable under the PPTA and 30% lower than the rate obtainable under CAP D3 LFN 2004.

But it must be borne in mind that, irrespective of whether a company is operating under the two zones as to be caught up by both tax band rates, all upstream petroleum operations companies are now subject to tax under CITA, which, in effect, places extra burden of 30% (the rate of tax payable under CITA) on all such companies. This ultimately conduces to the fact that an upstream petroleum company operating under both geographical zones will end up paying 110% tax; while the one operating under one zone will end up paying 80% or 60% tax, depending on which specific or particular zone the company is operating.

v. *Chargeable Tax*. Before 1999, the chargeable tax for an accounting period to be assessed, charged and paid is the amount of the assessable tax less tax offsets, which are all royalties due in respect of chargeable oil won and locally disposed off other than those deductible under section 10(1)(a) of the PPTA; all non-productive rents; and liabilities incurred by the company during the period to the Federal Government of Nigeria by way of customs or excise duty etc.[301] The current state of the law is that chargeable tax is the assessable tax less investment tax credit.[302] As for the other items, they have ceased to be tax offsets, but are now available as deductions from profit in computing adjusted profits for the relevant accounting period.[303] However, as we shall see under the Production Sharing Contract regime

[301] Ayua, op cit., p. 201.
[302] See section 22 of the PPTA.
[303] See section 10(1)(b), (c) and (d) of the PPTA. Perhaps it is because of this that Etikerentse argues that there is no longer chargeable tax, so that the basic amount representing a company's tax liability for any accounting period is its assessable tax. This is not correct, because chargeable tax is still very much obtainable under the PPTA as amended.

investment tax allowance and investment tax credit, two items with differing fiscal implications, are obtainable.

Under certain circumstances, additional chargeable tax may be assessed for due payment by the company for any relevant accounting period.[304] Etikerentse states that while assessable tax relates to a company's income under section 9(1) of the PPTA, additional chargeable tax under section 23 requires, on the other hand, the imposition of a posted price on the quantity of crude oil exported from Nigeria by the company during the period. Etikerentse finds justification for this provision, that is to say – the essence of providing for additional chargeable tax under certain circumstances is

> that if for any accounting period of a company the amount of the chargeable tax for that period is less than the posted price under section 23(3) and (4), the company shall be liable to pay an additional amount of tax; being the difference between the two amounts… The posted price is periodically revised in order to take advantage of the benefits dictated by favourable market conditions, as such long-standing commitments are not made by the NNPC.[305]

In other words, it is a provision aimed at shoring up the revenue base of the government. If it were not so, loss of revenue on account of the differences between the proceeds of sale arising from section 9(1) of the PPTA and the posted price would be monumental. Secondly, the provision will ensure that all avenues for revenue to the government are explored and exploited, especially these days in which the price of crude oil is an unstable as water.

3.1.5 Assessment under the PPTA

[304] See section 23 of the PPTA.
[305] Op cit, p. 258.

Pursuant to section 35 of the PPTA assessment can be in one of three ways: where the accounts submitted are accepted and assessments are based on the accounts by the FIRS; or where the accounts submitted are rejected and best of judgment assessment is to be raised; or where the company has failed to render accounts and other particulars and best of judgment assessment is to be raised. The PPTA provides for additional assessment, amended assessment, revised assessment and refusal to amend an assessment. For example, the FIRS has powers to make additional assessment if it discovers or is of the view that tax has not been charged and assessed upon the company or has been charged and assessed upon the company at a less amount than that which ought to have been charged and assessed for any accounting period of the company.[306] The PPTA requires that additional assessment shall be made within six years. To this requirement, it is submitted that it amounted to legislative approval of tax avoidance and tax evasion.

Further, the assessment must be in the form prescribed by the FIRS and must contain certain requisite particulars, for instance it must contain the names and addresses of the companies assessed to tax or of the persons in whose names any companies (with the names of such companies) have been assessed to tax, and in the case of each company for each of its accounting periods, the particular accounting period and the amount of the chargeable profits of and assessable tax and chargeable tax for that period.[307] Now the assessment must

[306] Section 36 (1) of the PPTA.
[307] Section 37 of the PPTA.

be served personally on or sent by registered post to each person whose name appears on an assessment.[308]

Although no assessment can be quashed or impeached on account of non-compliance with the form, since the law in taxation looks at substance, or because of mistake as to the name of a company liable or of a person in whose name a company is assessed; or the amount of the tax; by reason of any variance between the assessment and the notice thereof, it is submitted that the assessment must be duly served.[309] Otherwise, it will be impeached or affected on account of improper, or none, service. This is because due and proper service of assessment notice is a condition for recovery of tax.

3.1.6 The PPTA and Memorandum of Understanding (MOU)

The MOU is an agreement between oil companies and the NNPC, representing the Federal Government, representing a package of fiscal incentives to enhance crude oil export, encourage investments in exploration and development activities, encourage investments in enhanced oil recovery projects and encourage investments in gas utilization. It was commenced in 1986 and represented government's direct response to the oil glut of the 1980s. The object of the MOU, expected to last for five years, was to minimise the tax liabilities of the petroleum operations company. The MOU was supplemented by Side Letters from the NNPC.

(a) *1991 MOU*. A second MOU was executed in 1991. Albeit substantially the same in intent as that of 1986 MOU, it main features were increase in the guaranteed notional profit margin; improved technical cost entitlement; and

[308] Section 38 of the PPTA.
[309] Section 39 of the PPTA.

introduction of the reserve additions bonus (RAB) to show effective exploration effort as qualification for investment tax credit (ITC).[310] The concept of RAB sought to encourage investments in exploration and development activities and to enhance crude export. Thus, it was a tax incentive that could increase the crude reserve of an operating company in any accounting period, so that if the reserve so increased is confirmed by the DPR and approved by the Ministry of Petroleum Resources, the RAB would be granted as a deduction against the PPT liability for the year. According to Clause 2.9 of the 1991 MOU, the grant of RAB is subject to the extent that in any one year the additions to oil and condensate ultimate recovery exceeds the production for that year and then the company shall be entitled to a Reserve Additions Bonus. The fiscal implication of the RAB was availability of ITC as a set-off against the PPT for any company that met the condition attached to it. However, the RAB opened the flood gate of tax avoidance sophistry, leading to its discontinuance in the 2000 MOU.

(b) *2000 MOU*. This MOU revised the 1991 MOU. The purpose of the MOU include, among others, to provide incentives for enhancing crude oil exports, to provide assistance in the achievement of Nigeria's long-term growth objectives, to encourage cost efficiency, to provide encouragement for gas utilization activities, etc. Although outside the scope of this Research, the 2000 MOU contains, according to Etikerentse, "complicated formula for calculating what goes to the government in a fiscal year".[311] The 'complicated formula' relate to the determination of such items as 'capital investment expenditure',

[310] Arogundade, op cit. p. 228 and Etikerentse, op cit. p. 226.
[311] Etikerentse, ibid, p. 266.

'realizable price', 'notional fiscal operating costs', 'tax reference price', and 'tax inversion penalty', etc. For example, tax inversion penalty (TIP) seeks to encourage per unit cost efficiency by imposing a TIP at the rate of 35% per Clause 2.7 of the MOU. The TIP is determined by the operating cost, so that where the latter overshoots the threshold, the TIP automatically applies.

Under the regime of MOU, the tax rate is that spelt out by the MOU terms rather than the statutorily provided rate under the PPTA, which in itself poses legal puzzle. However, it would appear that the Supreme Court has resolved the issue when it stated that there is no doubt that the agreements are not illegal contracts because their terms vary the obligations of the operating companies to the Government under the PPTA nor are they against public policy.[312]

Conversely, the MOU is a disincentive to revenue accruable to the government. This obviously informed the observation of Etikerentse that "the fiscal attraction and incentives for an oil company to arrange its affairs in order for its profits to come within the application of the MOU as against the PPTA's strict provisions are still very much present". No wonder, joint venture companies chose to have their tax obligations subjected to the terms and conditions of the MOU. Further, it is submitted that the conditions which led to the MOU are no longer obtainable, especially with current rising oil prices – even though fluctuations are not unexpected. By and large, it should be discontinued. On the other hand, it is hoped that the PIB 2008 will scale through the legislative process, and when this is done, the era of MOU will have been closed finally since there is no simile provision in the Bill.

[312] See Shell Petroleum Development Company Nigeria Ltd v. FBIR (supra) and Solanke v. Abed (1962) 1 SC NLR 371.

3.1.7 Donations and Contributions under the PPTA

Under the PPTA, provision similar to or comparable with section 21 of the CITA does not exist. That is there is no specific provision under the PPTA which authorises donations and contributions and treats same as deductible or non-deductible expenses. Etikerentse reveals that the conventional practice of the oil companies recognised and approved by the FIRS "is that exemption granted by section 21 of the CITA[313] applies equally to the donations by oil companies", notwithstanding that the oil companies tend to direct their donations and contributions "more to causes, institutions and communities in their areas of operations and which are closely related to petroleum operations" being incidental expenses to petroleum operations.[314] The attitude of the FIRS is commendable, since it will leave no room for the oil companies to shirk responsibility.

3.1.8 Collection, Penalty and Interest Payments under the PPTA

By end of February of an accounting year, every company taxable under the PPTA must submit an estimate of the oil revenue for the year payable in twelve equal instalments, commencing from March and ending by the last day of February of the following year.[315]

Arogundade decried that the PPTA assumed that every petroleum operator is a good corporate citizen, because "non-payment of tax impose under sections 35 and 36 is not contemplated and sanctions are therefore not provided" accordingly.[316] The author went on to assert that "the payment of penalties

[313] See n. 246 at p. 88.
[314] Etikerentse, op cit. p. 280.
[315] Section 45 of the PPTA.
[316] Op cit. p. 263.

under section 46 applies to the non-payment of estimates provided under section 33 of the Act." It is also the contention of the author that the Act "does not provide for the payment of interest for late payment or arrears of taxes". The author regretted that "these deficiencies in the law (will) impede the enforcement or recovery of tax debts, especially among the sole-risk operators". With respect, the author misplaced his views. This is because **section 51 of the PPTA** took care of his fears. Hence, any person guilty of an offence against this Act or of any rule made thereunder for which no other penalty is specifically provided, shall be liable to a fine of N10,000, and in default of payment to imprisonment for six months. The question is not whether the law provides for penalty but the extent of it – whether the penalty under section 51 is grave enough to deter and discourage non-compliance. Having regard to the industry, it is submitted that the fine of N10,000 is to say the least paltry. It is thus submitted that the amount should be shored up so that even the contemplation of non-compliance will be far from the companies falling under the Act.[317]

3,2 THE PSC ACT (CAP D3 LFN 2004)

The PPTA is applicable under the PSC regime. However its application is, it is submitted, complemented by the PSC Act. Under the PSC regime, the contractor finances the operations while the concession holder shares in the profit. The applicable tax rate is a flat rate of 50% of chargeable profits.[318] An ITC of 50% of qualifying expenditure for contracts executed before 1/7/1998

[317] But see Part VI on Offences and Penalties, FIRS Act 2007, discussed in Chapter Five, where improvements have been made in the area of penalties.

[318] See section 3 of the PSC Act.

and investment tax allowance (ITA) for subsequent contracts are applicable.[319] Oil-blocks are ring-fenced so that a loss from one oil block cannot be set off against profits from another oil block.[320]

Payment of tax is in kind, by the allocation of tax oil to the NNPC for payment of PPT on behalf of both parties.[321] Royalty is also payable in kind, and in the following parameters:

TABLE 3.5

AREA	RATE
201 to 500m water depth	12%
501 to 800m water depth	8%
801 to 1000m water depth	4%
Areas in excess of 1000m water depth	0%
Inland Basin	10%

Undoubtedly, the regime of PSC is attractive both to the government and the contractor, oil companies. For the government, the burden of meeting cash call obligations which marred the JVC operations is eliminated. For the contractors, the tax liability is much reduced. In other words, it has a reducing effect on the revenue available to the government.

3.2.1 Qualifying Capital Expenditure under the PSC Regime

However there is a knotty issue under the PSC regime. It relates to PSC executed under section 22 of the PPTA and the PSC executed under the PSC Act. It must, at the outset, be pointed out that, as against the erroneous

[319] Section 4 of the PSC Act.
[320] Section 3 of the PSC Act.
[321] Section 9 of the PSC Act.

statement of Arogundade, the PSC Act is NOT an amending Act to the PPTA, so it cannot be said that the PSC Act elevated itself to a "status superior to that of the principal Act, the PPTA".[322] The knotty issue relates to ITC and ITA. Under the PSC Act, allowable ITC is 50% of qualifying capital expenditure for the accounting period that the asset was used and must have been incurred prior to 1/7/1998; and allowable ITA is equally 50% of qualifying capital expenditure for the accounting period incurred after 1/7/1998. On the other hand, section 22 of the PPTA[323] provides for deduction of ITC as 50% of chargeable profit, which is then deducted from assessable tax to arrive at chargeable tax for PSC under the PPTA. The ITC under the PPTA is deductible yearly for the duration of the PSC.

The implication of this, as shall be shown shortly, is that there is a world of difference between PSC executed under the PPTA as provided in section 22 thereof and PSC executed under the PSC Act, the principal Act on PSC regime. Arogundade points out that the tax effect of ITC is not the same as ITA in that both concepts have different effects in taxation. The effects are brought out in subsequent Tables 3.6, 3.7 and 3.8 below, adapted from Nigerian Income Tax and Its International Dimension, 2005.

FACTS: LPC LTD HAS AN ASSESSABLE PROFIT OF $2M. CAPITAL ALLOWANCES FOR THE PERIOD IS $250,000. EXPENDITURE ON QUALIFIED CAPITAL ASSETS IS $500,000. COMPUTE ITC AND ITA UNDER PSC REGIME AND ITC UNDER THE PPTA REGIME.

TABLE 3.6 – ITA under PSC regime

[322] Op cit, Arogundade, p. 241.
[323] This section is the result of Finance (Taxation Miscellaneous Provisions) Decree No. 30 1999

Particulars	Amount ($)	Amount ($)
Assessable profits (a)		2,000,000
LESS: Capital Allowances (b)	250,000	
LESS: ITA (i.e. 50% of $500,000 qualifying capital expenditure) (c)	250,000	500,000
CHARGEABLE PROFITS (d)		1,500,000
Assessable Tax (i.e. 50% of d)		**750,000**

TABLE 3.7 – ITC under PSC regime

Particulars	Amount ($)
Assessable profits (a)	2,000,000
LESS: Capital Allowances (b)	250,000
CHARGEABLE PROFITS (c)	1,750,000
Assessable Tax at 50% (tax rate is 50% flat rate of chargeable profits) (d)	875,000
LESS: ITC (i.e. 50% of $500,000) (e)	**250,000**
Chargeable Tax (i.e. d-e)	**625,000**

TABLE 3.8 – ITC under PPTA regime

Particulars	Amount ($)
Assessable profits (a)	2,000,000
LESS: Capital Allowances (b)	250,000
CHARGEABLE PROFITS (c)	1,750,000
Assessable Tax at 50% (tax rate is 50% flat rate of chargeable profits) (d)	875,000
LESS: ITC (i.e. 50% of c)	**875,000**
Chargeable Tax	**Nil**

ANALYSIS:

(i) From Table 3.6 ITA would yield higher tax liability of $750,000 compared to $625,000 tax liability chargeable under ITC in Table 3.7. However, both are under PSC Act. The point of difference between ITC and ITA is the point at which each is applied. For instance, as can be seen from the tables, ITC is deductible from assessable tax while ITA is deductible from assessable profits.

(ii) A funny but regrettable situation showed up in Table 3.8, that is ITC under PPTA regime. One, ITC is a percentage of chargeable profits. Two, it is then deducted from assessable tax in order to arrive at chargeable tax, which will represent tax due to be paid. Because of this, LPC Ltd is left with nil tax payable. Although the resulting absurdity is the natural consequence of section 22 of the PPTA, it cannot be said to be representing the legislative intent, which is targeted at a mischief. In fact, the section requires the deduction to be continuous for any accounting period for the duration of the contract: if the contract is made to last for 10 years and qualifying capital expenditure are successively incurred, the contractor could get away with non-payment of PPT. What an absurdity!

(iii) A strict interpretation of section 22 of the PPTA PSC provision would yield manifest absurdity. Therefore, it is submitted that the PSC Act provision is to be preferred. This position is strengthened by the PSC itself: one, ITA and ITC are deductible once; two, the PSC is subject to review to ensure that if the price of crude oil at any time exceeds $20 per barrel, in real terms, the share of the Government of the Federation in the additional revenue shall be adjusted

under the Production Sharing Contracts to such extent that ensures the Production Sharing Contracts shall be economically beneficial to the Government of the Federation.[324]

(iv) The seeming confused state of affairs, as regards the appropriate and operative tax regime, appears to be serving the interest of international oil companies, who have waged a campaign of calumny, pervasion and truncation against the Petroleum Industry Bill 2008.[325] Happily, investment tax credit has been removed from the PIB, if it passes into law. Without more, it cannot be said that it was intended that no tax liability should result at all after netting off ITC from assessable tax. This point leads to the inference below:

(v) From the foregoing, there is apparent inconsistency between the section 22 provisions on PSC of the PPTA and the provisions of the PSC Act. Recourse to rules of construction will solve this problem. Although, repeal by implication is not favoured generally, this is a case in which repeal by implication is favoured. Thus, it has been held that where the provisions of a later enactment are so inconsistent with or repugnant to the provisions of an earlier one that the two cannot stand together, the earlier is abrogated by the later.[326] Thus section 22 of the PPTA, it is submitted, can be taken to have been abrogated by the PSC Act. Stamping this view, the PSC Act provides that if the provisions of any other enactment or law are inconsistent with the provisions of this Act, the provisions of this Act shall prevail and the provisions of that other enactment or law shall, to the extent of that

[324] Section 16 of the PSC Act. Like provision is contained in the Petroleum Industry Bill 2008.
[325] See Chapter Two, p. 52 above.
[326] See Kutner v. Phillips (1891) 2 QB 267, per Smith LJ; Flannigan v. Shaw (1920) 3 KB 96 per Scrutton LJ.

inconsistency, be void.[327] With due respect therefore, the strenuous orchestration of legislative faux pas and gaffe by Arogundade is therefore a chasing after the wind and academically benighted.

3.2.2 Collection and Payment Procedure under the PSC[328]

Under the PSC regime the NNPC as the concessionaire or concession holder collects the tax oil, sells and remits it in designated foreign bank accounts.[329] Arogundade made a sound observation to the effect that section 14 of the PSC Act limits the role of the FIRS to issuance of receipts as advised by NNPC, the concession holder. This position was addressed in the Petroleum Industry Bill 2008, which provides that tax oil shall be allocated to the FIRS which shall elect to collect the tax due either in kind or in cash. In issuing receipts, the FIRS shall issue two separate receipts one bearing the name of the concession holder and the other bearing the name of the contractor. The receipts as issued by the Service shall bear the names of each Party as defined in the PSC in accordance with each Party's tax oil allocation for the payment of petroleum profit tax under the provisions of the PSC.[330]

3.2.3 Criticisms of the PSC Act

The PSC Act has been criticized on the ground that it relegated the FIRS "to the status of a mere post office" against its statutory role of assessment, collection and accounting. The PSC Act is said to be silent on assessment, implying that the Act "expects the companies to obey the law by filing returns for assessment purposes".[331] Thus, while it is conceded that the relegation of the

[327] Section 15 of the PSC Act.
[328] See further, Chapter Five, infra.
[329] Section 9 of the PSC Act.
[330] Section 14 of the PSC Act.
[331] Arogundade, op cit. p. 242.

FIRS to the background is a well founded shortcoming of the Act, this cannot be the case for assessment. It should be remembered that the Act does not intend to supplant the PPTA. In so far as the PPTA is not inconsistent with the Act, the provisions of the PPTA in section 35 apply mutatis mutandis to the PSC Act. The PSC Act says itself in section 15(1). Further the newly enacted FIRS Act 2007[332] appears to have significantly whittled down this weakness.

Under the PSC regime, there is ring-fencing of oil wells. This means that taxation is based production per contract area, so that a "loss from one oil block cannot be carried into the profit from another as an offset." Carryover of losses is allowed under the PPTA that is JVC operators. Thus if a taxpayer under PPTA incurs loss in any accounting period, it can be carried forward to the succeeding accounting period and deducted from the adjusted profits in order to arrive at assessable profits for the relevant accounting period.[333] This point is criticism which favours the contractors, but an ingenious mechanism of which the government will take pride in.

Moreover, it is submitted that since the allocation of cost oil to the contractor in such a quantum as to generate an amount of proceeds sufficient to cover operating costs is shrouded in secret dealings between the NNPC and the contractor, the process is anything but transparent. On this point, Arogundade queries, "who monitors the pre-production expenses being incurred by the company? Who keeps the books?" To ensure that the government and people of Nigeria are not short-changed under the cloak of PSC regime, it is submitted

[332] See Chapter Five, infra.
[333] See p. 92 above.

that regular returns should be filed with the FIRS so that they are kept abreast of activities of the contractor.

3.3 THE INCENTIVES ACT

The Incentives Act is applicable to natural gas operations, but more specifically to the Nigerian Liquefied Natural Gas Company of Nigeria Limited. The provisions of the Act are slavishly skewed in favour of the NLNG, which in the final analysis is to the benefit of foreign partners. One, the NLNG is granted pioneer status under the Act, meaning that it had enjoyed tax heaven of five years.[334] It is submitted that by carefully excluding the application of section 10 of CAP I79, the Incentives Act provided a 10-year tax holiday.[335] Also, the applicable tax regime as far as the NLNG is concerned is the CITA, notwithstanding that the NLNG is well within with the purview of the PPTA, and should have been taxed thereto[336].

As if not enough, the Act excluded the application of the provisions of the **National Shipping Policy Act CAP N75 LFN 2004 (now repealed by Nigerian Maritime Administration and Safety Agency Act, No. 17 2007)** to the NLNG Limited and its contractors. In other words, "there is no room for participation of Nigerians in the shipping trade as it affects the operations of the NLNG".[337] This latter provision is unjustly tilted in favour of foreign interests. It is tantamount to economic disenfranchisement of Nigerians. In fact, it would appear that the NLNG and its foreign contractors are more favoured under the liberalised economic climate. This is because the NLNG

[334] See section 10 Industrial Development (Income Tax Relief) Act, CAP I79 LFN 2004.
[335] See section 2 of the Incentives Act.
[336] See section2, PPTA for definition of petroleum operations.
[337] See Onamson., ibid, p. 31.

reserves the right to elect whether to transact with Nigerians or not. Until this law is amended, it is doubtful whether the newly enacted **Nigerian Oil and Gas Industry Content Development Act 2010,** will be of any use here.

In addition, the second schedule to the Incentives Act carefully and imperviously provides that the Federal Government of Nigeria grants guarantees, assurances, and undertakings which shall have the effect from the date hereof and so long as the company (NLNG) or any successor hereto, is in existence and carrying on the business of liquefying and selling liquefied natural gas and natural gas liquids within and/or outside the Federal Republic of Nigeria. Fortifying this latter provision, the government amongst other things binds itself not to amend the fiscal regime contained in the Act, except with prior written agreement of the shareholders, NLNG and itself. The NLNG and its shareholders shall not be subject to new laws, regulations, taxes, etc which are not generally applicable to companies incorporated in Nigeria. That is, it cannot, for example, be subject to PPTA, since the PPTA is not generally applicable to all companies incorporated in Nigeria. It is submitted that the provisions of the Incentives Act are overly repugnant, nauseating to sensibilities of Nigerians, obviously contrary to equity, justice and good conscience and incongruently inconsistent with public policy. Incidentally, but regrettably, the Incentives Act was not slated for repeal under the Petroleum Industry Bill 2008.

In a nutshell, the Act, it is submitted, has served out its usefulness. One, the Incentives Act appears to be an instrument of fraud, especially when it is considered against the backdrop of NNPC's claim that it had no record of

natural gas produced or sold by the NLNG after close to 10 years of its operation.[338] Two, the Petroleum Industry Bill removed incentives for utilization of associated and non-associated gas under the PPTA regime.

3.4 OTHER FISCAL MATTERS RELATING UPSTREAM OPERATIONS

Other fiscal matters discussed hereunder constitute, with equal force like the various tax regimes already examined and analysed, major sources of income to government from upstream petroleum operations. They are Bonuses, Fees, Royalties and Oil Terminal Dues, etc.

3.4.1 Bonuses.

These are premiums payable which represent monetary consideration for grants of OPL, PSCs and marginal field allocations. Etikerentse, questions the fairness in the "demand for bonuses for marginal fields allocations" made payable to the government when it is considered that a bonus had earlier been paid by the main farmor on the concession and that the lease being farmed into does not belong totally to the government. With respect, a marginal field is a non-producing field or a field which the concession holder has left unproduced due to the economics of production attending to the concession area. In order to encourage local participants the government withdraws the concession from the holder and allocates to a willing producer, normally Nigerians. Thus, the allocation is by government and one should not lose sight of the constitutional provision which vests rights and ownership of mineral resources in the government of the federation.

[338] See, n. 153 p. 50 above.

The value of the premium, paid either on the OPL or PSC, is dependent on the size of the concession area and it must be made in hard currency and within the time stipulated in the grant. Time of payment is of the essence as failure to pay within the time allowed for payment "would vitiate the grant except an extension period is permitted".[339] While application fee is payable to trigger the process of converting an OPL into OML, no premium is required to so doing.

3.4.2 Fees.

Some fees are payable in respect of an OPL and OML and they constitute fiscal outlay to the government.[340] For instance, application fee for an OPL and OML is $10,000 and $500,000 respectively; processing fee for an OPL application is $10,000; application to withdraw any application earlier made is N20,000, while application to terminate or effect partial surrender of an OPL or OML is N50,000, among other fees. Under Regulation 30A, an application fee of N5,000 is payable in respect of the permit granted by the DPR which is required by a lessor for conducting seismic data survey.

Additionally, Regulation 60A of Petroleum (Drilling and Production) Regulations detailed fees payable in respect of support services. For instance, under General Purpose Category Services, application fee is N5,000 and renewal fee is N5,000, while for Specialised Category application fee is N250,000 and renewal is N250,000. The above fees are not exhaustive but an attempt to show its existence.

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[339] Etikerentse, op cit. p. 268.

[340] See Paragraph 30 First Schedule to the Petroleum Act and Regulation 58 (Part VI) of the Petroleum (Drilling and Production) Regulations (as amended in S.I. No. 3 2001).

3.4.3 Royalties.

Royalty in the oil industry "is meant to be the landowner's share in kind of the petroleum produced from the concession area, free of producer's production expenses".[341] However, in the case of Nigeria royalty is that sum of money that is payable by the producer on the quantity of the oil produced at the percentage fixed by law and can by paid wholly or in part, in kind to the government.[342]

Section 2 of the PPTA defines royalty as the amount of any rent as to which there is provision for its deduction from the amount of any royalties under an OPL or OML to the extent that such rent is so deducted; and the amount of any royalties payable under such licence or lease less any such rent deducted from those royalties.[343] For example, royalty of 20% of the chargeable value of the crude oil and casing head petroleum spirit produced from the relevant area in the period is payable for on-shore production, while it is 18.5% for production in territorial waters and continental shelf areas of up to 100 meters water depth, etc.

On royalty, Etikerentse notes that (1) the time for the payment of royalty shall not be more than one month after the end of every quarter including the quarter in which the payer's licence or lease becomes effective, or otherwise as the Minister may direct; (2) with respect to determination of the 18.5% royalty rate area of application, Nigeria's territorial waters means any part of the open sea within twelve nautical miles of the coast of Nigeria, measured

[341] Etikerentse, op cit. p. 269.
[342] See Paragraph 32, First Schedule to the Petroleum Act.
[343] Paragraph 32, First Schedule to the Petroleum Act provides the requirement for royalty payment; while Regulation 60(1) of the Petroleum (Drilling and Production) Regulations specifies the rates.

from low water mark or of the seaward limit of inland waters;[344] and (3) all royalties the liability for which was incurred during the relevant accounting period are deductible expenses under section 10(1)(b) of the PPTA.[345]

3.4.4 Oil Terminal Dues.

This class of payment is required to be made to the Nigerian Ports Authority (NPA) for all oil evacuated from oil terminals pursuant to Oil Terminal Dues Act CAP O8 LFN 2004 and **Nigerian Ports Authority Act, CAP N126 LFN 2004**. To this effect, section 1 of the Act provides that terminal dues may be levied on any ship evacuating oil at any oil terminal for any services or facilities furnished by the NPA under the Act.[346] Under the Act, the master or owner of the ship or every consignor or agent who has paid or made himself liable to pay any dues on account of such ship are persons liable to pay any levied terminal dues on ships evacuating oil at a terminal.[347]

It is important to bear in mind that oil terminal dues do not qualify as deductible expenses under the PPTA. The reasons are not far-fetched. One, it is the ship master or owner and not the company that won and sold the oil. Two, **section 12 of the PPTA** excludes matters relating to transportation of chargeable oil by oceangoing oil tankers.

[344] See section 18(1) Interpretation Act.
[345] Op cit. pp. 270-271.
[346] Section 7(3) defines Oil Terminal.
[347] See section 1(2) of the Act.

CHAPTER FOUR

FISCAL LAWS RELATING TO DOWNSTREAM OPERATIONS

4.0 INTRODUCTION

Historically, "taxation of companies started in 1912 which was followed by a series of amending Acts".[348] Even during this period companies were taxed under the normal income tax legislation so that it was not distinct and separate from taxation of sole traders or partnerships.[349] This explains why there are still "many similarities in the way in which companies are taxed under corporation tax rules compare to sole traders and partnerships that continue to be subject to income tax".[350] It was not until 1961 that a comprehensive system of corporation taxation was introduced in Nigeria.[351] Even under the CITA 1990, the structure of corporate tax has remained substantially unchanged when compared to its predecessor Acts.[352] Nigeria has oscillated between the classical system, and imputation system, of corporation tax, though the former is currently in use in Nigeria.[353] It must be noted that in 2007, Part I of the CITA was repealed and promulgated as Federal Inland Revenue Service (Establishment) Act 2007 (hereafter the "FIRS Act"),[354] but this did not affect the structure of corporate taxation but established the FIRS as a separate body with fiscal administrative

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[348] Ayua, op cit, p. 163.
[349] Companies were similarly charged to tax under the Income Tax Ordinance of 1948, which codified the 1943 Ordinance and subsequent amendments.
[350] Lymer A., and Oats L., **Taxation: Policy and Practice**, 12th edition (200/06), Birmingham: Fiscal Publications (2006), p. 289.
[351] Ayua, ibid; Arogundade, op cit, p. 161.
[352] That is, Companies Income Tax 1961 and Companies Income Tax Decree 1979.
[353] See, Lymer and Oats, op cit, pp. 290-291; Arogundade, op cit, p. 269.
[354] See section 62 FIRS Act and section 2 Companies Income Tax (Amendment) Act 2007.

powers over certain taxing Acts.[355] Yet, the Companies Income Tax (Amendment) Act 2007 (hereafter "CITA 2007") did not affect the structure of corporate tax.

Under the CITA, a company, whose profits are chargeable to tax, is any company or corporation, other than a corporation sole, established by or under any law in force in Nigeria or elsewhere.[356] This definition affects all companies, yet not all companies are covered by the Act which defined it. Thus, CITA governs taxation of profits of companies not specifically subject to upstream petroleum operations in Nigeria.[357] However, in the Nigerian petroleum industry two broad sectors are easily identifiable, to wit upstream sector and downstream sector.[358] However, the latter sector is not subject to tax under the PPTA, but under the CITA. Having regard to our extensively inclusive definition of petroleum operations in this Research, downstream sector falls under petroleum operations. Accordingly, this Chapter is concerned with downstream petroleum activities companies whose profits are chargeable to tax under the CITA and not under PPTA. It is this nexus that has led to a critical consideration of CITA as a fiscal law relating to petroleum operations in Nigeria.[359]

4.1 CONSTITUENTS OF DOWNSTREAM OPERATIONS

The core activities involved in the downstream sector of petroleum operations in Nigeria and falling within the purview of the CITA have been identified to consist of transportation of crude oil by ocean going tankers from Nigeria to another country; oil refinery; oil distribution and marketing; servicing operations in the

[355] See s. 8 and s. 25 of the FIRS Act.
[356] See section 105 CITA 2004.
[357] As noted earlier in the previous, upstream petroleum companies are subject to PPTA.
[358] But see the PIB 2008 where we now have upstream, midstream and downstream sectors.
[359] Accordingly, capital gains, investment incomes and deemed incomes are beyond the scope of this Research and will therefore not be considered.

upstream sector; and utilisation of associated and non-associated gas [360]. These activities, save transportation, are taken together.

(i) **Transportation of Crude Oil.** Under the PPTA, evacuation of crude oil by ocean going oil tankers operated by or on behalf of an upstream petroleum company from Nigeria to another territory is excluded from PPT.[361] By this exclusion, profits from the oil transportation business will be taxed under the CITA 2004. Three types of transportation as far as evacuation of crude is concerned have been identified, namely:

> (a) where the upstream petroleum operator has his own ship for the transportation of the crude to his refinery or to the spot market;
> (b) where the operator, like the NNPC, has no ships of his own but allows buyers of the crude to bring their own ships for the evacuation of the crude; and
> (c) where the buyer or the operator has no ship of his own but hires ships for the transportation of the crude.[362]

In (a) above, the operator is involved in a separate and distinct business in Nigeria. The profits from this business will be chargeable to tax under the CITA. In (b), section 14 CITA 2004 relating to companies engaged in shipping or air transportation, will be used in determining the profit of the business: in which case the higher between the deemed profit or minimum tax of two percent will apply. A further two percent "withholding tax will be applicable to each payment for the lifting"[363]. In (c), the payment to the hirer (the owner of the ship hired) amounts to rent, and this makes the CITA applicable.[364] Thus, the buyer or the operator expectedly will

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[360] Arogundade, op cit, p. 159.
[361] See section 14 PPTA 2004; **Shell-BP Petroleum Development Company of Nigerian Ltd v. Federal Board of Internal Revenue** (supra).
[362] Arogundade, ibid.
[363] Ibid.
[364] Section 79 CITA 2004, particularly see subsection 6 thereof.

withhold tax from the payment at the applicable rate of 10%. As to the enforcement of payment of tax under this head, the FIRS has a remedy.[365]

(ii) **Other Downstream Activities.** Oil refining is a manufacturing activity, and the profit therefrom is assessable to tax under the relevant charging section of the CITA.[366] The key players in oil distribution and marketing are the NNPC with its 'mega stations', the major and independent marketers in the sale of refined crude, the profits of which are chargeable to tax under CITA. Gas utilisation is equally treated as lownstream operation, and according to the CITA it is the marketing and distribution of natural gas for commercial purpose and includes power plant, liquefied natural gas, gas to liquid, fertilizer plant, gas transmission and distribution pipelines.[367]

Further, oil servicing activities include "surveys, drilling, catering, hire services, finance, supp of equipment, property and know-how and other forms of technical, consulting or management services".[368] The beneficiaries of these services are upstream operations companies. Under CITA oil servicing, activities, though carried on by the same company, may be differently characterised for tax purposes. This means that under the CITA different rates may apply. Insightfully helpful examples will include:

> the profits of the company (i.e. oil servicing company) engaged in consultancy, installation, construction, building, delivery or technical services would be captured as business profits; hire of equipment or facilities is taxable as rent; the returns from the financial transactions is taxable as interests; and the payment for know-how, patent, license and other rights would attract tax as royalties (emphasis added).[369]

[365] Section 87(4) CITA 2004. The issue of administration of the fiscal laws is explored in Chapter 5.
[366] See section 9(1)(a) CITA 2004.
[367] Section 39 CITA 2004. Incentives are provided for companies under this activity, discussed infra.
[368] Arogundade, op cit, p. 160.
[369] Ibid.

4.2 CHARGE TO CORPORATE INCOME TAX[370]

Corporate income tax is chargeable on the profits of any company accruing in, derived from, brought into or received in Nigeria from any or all of the following sources:

i. Trade or business;
ii. Rent or premium;
iii. Dividends, interests, discounts, royalties, charges or annuities;
iv. Annual profits or gains not falling within the preceding categories;
v. Deemed profits;
vi. Service fees, dues and allowances; and
vii. Profits from dealings in securities.

Understandably, different provisions of the law apply to the above sources; hence different principles apply in the determination of payable tax. To be able to appreciate the differences, the sources that fall under the assessment principles and provisions of the law would be grouped together, that is matching likes with likes. Thus, "business profits" would include "the profits from trade or business, services, receipts that are of revenue nature and receipts from dealings in securities".[371] The other category of taxable profits of a company is "investment incomes" which include dividends, interests, rent and royalties. Lastly, there is the category of taxable profits from "deemed income" derivable from "businesses partly carried on in Nigeria and partly

[370] Section 9 CITA 2004; Arogundade, op cit, p. 166; Ayua, op cit, p.167; Abdulrazaq, op cit, pp. 124-125.
[371] Arogundade ibid.

elsewhere and would include profits from operations of international shipping and air transportation, profits from cable and wireless, profits from insurance business partly carried on in Nigeria and partly abroad".[372] For the scope of this research, discussion will dwell largely on business profits, and where the circumstances permit, investment income with respect to rent.

As noted above, tax is charged on the profits of a company which accrued in, derived from or brought into or received in Nigeria in respect of trade or business. To be able to identify what is a profit of the company, we must (a) discover what is trade or business from which the profit flows; (b) what is business receipt, and which aspect of a business receipt is subject to corporate tax; and (c) who is chargeable to corporate tax. However, it must be observed that on what "constitutes trade or business, adjustments for allowable and disallowable expenses, determination of assessable profits, returns filing, assessment and appeal procedures and collection procedures are similar"[373] under the CITA and the Personal Income Tax Act, 2004.

(a) **<u>Business or Trade</u>**. Although the CITA did not furnish any definition of the words "trade" and "business", the latter has been defined to include a trade, profession, or vocation.[374] As to trade, no definition was provided either in the CITA or the PITA. From the PITA definition of business, trade is an activity within a business. Particularly, trade has been said to encompass the totality of commercial activities which are "the winning and using the products of the earth, or multiplying the products of the earth and selling them, the purchase

[372] Arogundade, ibid.
[373] Arogundade, op cit, p. 130.
[374] Section 7(3)(a) Personal Income Tax Act, CAP P8 LFN 2004 (hereafter PITA).

and sale of commodities or the offering of services for a reward."[375] On the other hand, it has been suggested that the word trade should be construed from its "ordinary meaning", so that if "an isolated transaction is of a commercial nature, then it comes within the meaning of the word trade."[376] This water-tight approach to the construction of the word trade by the Nigerian courts is obviously different from the approach of the English courts. For instance, it has been held that the fact that the previous owner of a business was carrying on a trade "was not a conclusive evidence of a trade";[377] and the fact "that an activity generates a surplus will not necessarily turn that activity into trading".[378] Further, in **Leeming v Jones[379]** it was held that unless an isolated transaction for purchase and resale of property could be brought within case 1 of Schedule D as being an adventure in the nature of trade, it could not be assessed to income tax at all. But under the Nigerian jurisdiction such transaction, without doubt, can be assessed to income tax.[380]

Generally, it has been submitted that the courts would favour an examination of the "facts and circumstances of every transaction" in order to discover if the transaction bears any of the badges of trade as to make the profits flowing therefrom amenable to taxation.[381] Notwithstanding the recourse to the concept of badges for a determination of what constitutes a trade, **Bret LJ** states insightfully that "where a person habitually does and contract to do a thing capable of producing profit and for the purpose of producing profit, he

[375] Per Lord Atkin, in **Fry v Burma Corporation Ltd** (1930) 15 TC 113 at 114.
[376] Per Sowemimo J. in **Arbico Ltd v FBIR** (1966) 2 All NLR 303.
[377] See **Glasgow Heritable Trust Ltd v IRC** (1954) 35 TC 196; Arogundade, ibid.
[378] **Building & Civil Engineering Holidays scheme Management Ltd v Clark** (1960) 39 TC 12.
[379] (1930) 1 KB 279; 15 TC 333.
[380] See **Arbico Ltd v FBIR** (supra); **Aderawe Timber Company v FBIR** (1969) 1 All NLR 242.
[381] Arogundade, op cit, p. 131. For detailed discussion of the concept of badges of trade as enunciated by the **Royal Commission on the Taxation of Profits and Income** in its Final Report (Cmmd 9474 of June 1965) see Arogundade, op cit, pp. 131-134; Abdulrazaq, op cit, pp. 55-58; Ayua, op cit, pp. 96-102.

carries on a trade or business".[382] In this light, it is submitted that the activities of companies engaged in downstream petroleum operations are easily discernible that they scarcely admit of doubts or arguments as to their nature. This is because they can be gleaned easily from the company's constitutional document, the Memorandum of, and Articles of, Association.

Thus, the business of petroleum marketing companies involves trading in refined petroleum products; there are servicing companies whose business involves procurement, maintenance of facilities and infrastructure deployed to rigs by upstream petroleum operations companies; and yet there are others whose business border on services which may be technical, consultancy, agency, management or contract. All these activities, normally contained copiously in the objects clause of such companies, whether trading activity or services activity, are subject to corporate tax. However, it must be noted that the tax treatment of trade receipts and service receipts[383] are not the same. The major difference is that "service receipts (fees) are subject to source deductions whereas business receipts are not subject to withholding since they do not come under the source deduction rules"[384] under **section 94 of CITA 2004**. Reasserting the earlier submission, **Ayua** concludes that in determining whether a particular activity constitutes trading for purposes of corporate income tax, one of the factors, among others, to be considered is "the object clause of the Memorandum and Articles of Association".[385]

[382] **In Ericksen v Last** (1881) 8 QBR 915
[383] Business in line with the statutory definition provided above will include trade activity and service activity.
[384] Arogundade, op cit, pp. 166-167.
[385] Ayua, op cit, p. 169.

(b) **Business Receipts**. The business receipts of a company may be of two types: revenue in nature or capital receipts. The former is assessable to tax as a source of income, while the latter is not. This being the case, it means, naturally, that the two must be distinguished. Thus, **Lord Green,** points out that recurrence quality or nature of payments or receipts is the "distinguishing mark differentiating an income payment" for tax purposes.[386] In another case, it was held that the lump sum payment to a company to surrender its right to annual royalty payments amounted to capital receipts.[387] Yet in another case,[388] the joint-cooperative business agreement between a Dutch and a British company was terminated due to war. Prior to this, payments made under the agreement to the British company were treated as income and accordingly assessed to tax. The final payment preceding the termination of the agreement was held to be capital receipts.

From the above cases, revenue receipts assessable to tax are (a) receipts that recur as against those that are once and for all receipts which are capital; (b)a lump sum payment which amounted to surrender of the congeries of rights under a joint operating agreement, being a capital receipt, is not assessable to corporate tax; and (c) it is a capital receipt any payment receipt received for the termination of a contract agreement which effectually affected the whole profit-making outfit of the taxpayer, such a termination agreement not being an ordinary commercial contract made in the ordinary course of business. The distinction between capital receipts and revenue receipts is important because capital receipts are taxed under a separate taxing statute, the **Capital Gains**

[386] **Asher v London Film Production Ltd** (1944) KB 133 at 140.
[387] **British Borneo Petroleum Syndicate Ltd v Cropper** (1969) 1 All ER 104.
[388] **Van den Berghs Ltd v Clark** (1935) AC 431

Tax Act[389]; while revenue receipts are properly taxable under the CITA. Following this latter submission, gains from foreign exchange transaction could be treated as revenue receipt or capital receipt. Accordingly exchange gain would be assessable to tax if the gain arose from a loan in respect of revenue of the taxpayer; but it would be capital receipt if the gain arose from a loan to enable the taxpayer acquire capital asset.[390] The former is outside the scope of this Research. Our concern is with the latter, and this section of the Research focuses on that as it relates to downstream petroleum operations.

(c) **Exempted Profits**. Generally the profits of downstream operating companies are subject to corporate tax.[391] However, there are certain situations in which the profits of a downstream company may be exempted from payment of corporate tax. Thus, where any Nigerian company operating in the downstream industry is engaged wholly in export oriented business, its profits shall be exempt from corporate tax in respect of goods exported from Nigeria, provided that the proceeds from such export are repatriated to Nigeria and are used exclusively for the purchase of raw materials, plant, equipment and spare parts; or dividends from investments in wholly-oriented export business.[392]

An example of the above is not hard to find: hence, where a downstream company has made investments in a company whose products are wholly exported, the dividends from such investment are exempt from tax; or where a downstream company engages wholly export business (for instance, refining petroleum products or production of petrochemical products for export only),

[389] CAP C1 LFN 2004.
[390] By the authority of **UDT Bank (Nig) Ltd v FBIR** (unreported) APP/COMM/237 (1976).
[391] But the profits of statutory or registered friendly society, the profits of any company being a cooperative society, the profits of any company engaged in ecclesiastical work, charitable or educational activities, etc are generally exempted from corporate tax, see section 23 CITA 2004.
[392] See section 23(1) CITA 2004.

and uses the proceeds from the export to purchase raw materials, plant, etc for reinjection into its manufacturing process, the profits are exempt from tax. Further on this, the president may by order exempt any company or class of companies from all or any of the provisions of this Act; or from tax all or any profits of any company or class of companies from any source. The president is empowered to take this course or to exercise this power on any ground which appears to him or her sufficient.[393]

Additionally, **the Companies Income Tax (Amendment) Act 2007**[394] has added to the list of exempted profits of downstream companies operating in Nigeria. Accordingly, the profits of any downstream petroleum company established within an export processing zone or free trade zone, for instance the export processing zone in Calabar, shall be exempted from corporate tax. This new provision is however with a caveat: provided that 100 per cent production of such downstream company is for export. If this is not the case, then corporate tax shall accrue proportionately on the profits of the company.[395] From this provision, a downstream petroleum company that is engaged in petrochemicals, which products are wholly produced for export shall be exempt from payment of tax. However, another downstream company engaged in production of petrochemicals partly for export and partly for local consumption shall pay proportionate tax. The tax is proportional because it is the part of the production consumed or distributed locally that will attract tax.

[393] Section 23(2) CITA 2004.
[394] Hereafter, CITA 2007.
[395] Section 5 CITA 2007.

While the grounds for exemption from corporate tax of the profits or dividends from export related business of downstream companies can be appreciated, in that it is meant to encourage the development of the country's industrial base and generate employment, leading generally to the development and sustenance of a robust economy. However, the same cannot be said of the provision allowing the president to exempt on any ground which appears to him/her to be sufficient. It is submitted that this provision can be unduly exploited by any person occupying the office of the president who is not guided by the principles of integrity, fairness and equity. This point is to be appreciated when it is considered that there is no definition of what circumstances would be a sufficient ground. Where there is abuse, which apparently should not be unexpected, the country suffers, in that needed revenue will have been lost to personal pockets.

(d) **Chargeable Person**. The person chargeable to corporate tax is the company in its own name; or in the name of any principal officer, attorney, factor, agent, or representative of the company in Nigeria in like manner to like amount as such company would be chargeable; or in the name of a receiver or a liquidator, or of any attorney, agent or representative thereof in Nigeria in like manner and to like amount as such company would have been chargeable if no receiver or liquidator had been appointed.[396] Even the FIRS has power of appointment, and where such power is exercised the person so appointed shall be the agent of such company for the tax purposes and may be required to pay any tax which or will be payable by the company from any moneys which may be held by him for, or due by or to become due by or to become due by him to, the

[396] Section 47 CITA 2004.

company whose agent he has been declared to be and default of such payment the tax shall be recoverable from him.[397] This provision, it is submitted, strikes at avoidance tendencies of companies. The principal officer or manager in Nigeria of every company shall be answerable for doing all such acts, matters and things as are required to be done by virtue of this Act for the assessment of the company and payment of the tax.[398]

4.3 BASIS OF ASSESSMENT

Unlike the actual year basis applicable to upstream petroleum companies under the PPTA, the basis of assessment for downstream petroleum companies "is the income of the year preceding the year of assessment, that is to say business profits of downstream companies are taxable on preceding year basis".[399] The assessment runs from 1st January to 31st December, albeit a company may elect to choose its own accounting period "which is normally a 12-month period ending on a date in a year immediately preceding the assessment year".[400] For example, the profits to be assessed of XYZ Petroleum Refining and Marketing Limited in 2010 assessment year is the profit of the company earned, derived or accrued in the 12-month period ending in a date in 2009 accounting year. In other words, if the fiscal year end of the company

[397] See section 49 CITA 2004.
[398] Section 48 CITA 2004.
[399] Section 29(1) CITA 2004; Ayua, op cit, p. 174; Arogundade, op cit, p. 173.
[400] Arogundade, ibid.

is 31 December, it will have to forward its returns of income for the year 1 January to 31 December 2009 to the tax office for 2010 assessment year.[401]

It has been submitted that in line with the World Bank Report[402] that the preceding year basis of assessment should be replaced by current year system of assessing business profits. The reasons for this submission are two: one is inflation. The preceding year basis is "tantamount to the government giving taxpayers an interest-free loan", so that in times of inflation the government would not only lose the interest but also the value of the currency would have declined.[403] The second ground is for equity. Thus, the lag in the payment under the preceding year basis creates "inequities between taxpayers[404], wage earners and others subjected to withholding tax" that are under compulsion of law to pay their taxes on a timely basis.

The implication of the above submission is that it is "paper profits" rather than "real income" that are taxed in Nigeria. Thus, the current year system obtainable under the PPTA is to be preferred. Under this system, the upstream company has two payment options, all of which are based on current year basis: first, the taxpayer **provisionally** pays one hundred per cent of previous year's tax; or eighty per cent of current year's tax estimate is paid. The payments are on quarterly basis, meaning there may be a fifth quarter's payment when returns are made and payments reconciled. However, it has been correctly submitted that the workability of this system, which is capable of compelling self-assessment filing, is hinged on the law being reviewed and

[401] However, it should be noted that there are variances of this rule for downstream companies commencing business newly and those ceasing business, see proviso to s. 29(2) CITA and s. 29(4) CITA 2004.
[402] See Report No. 8361, UNI of 29 June 1990.
[403] Arogundade, op cit, p. 174.
[404] Especially between the downstream companies and upstream companies.

the FIRS better "equipped in terms of capacity building and provision of facilities".[405]

[405] Ibid.

4.4 ASCERTAINING ADJUSTED PROFITS OF DOWNSTREAM COMPANIES

It should offhandedly be supposed that the computation and ascertainment of profits of downstream companies should be based on the financial returns of a company and in line the "correct principles of the prevailing system of commercial accountancy."[406] However, this is not always the case. One each company has its own internal valuation policy, which if applied using "the prevailing system of commercial accountancy" will nevertheless result into different profitability situations. Two, there is the tendency of companies to play around with figures, and as **Cardozo J** pointed out, more often than not the profits of downstream companies

are not susceptible of ascertainment with certainty and precision except as the result of inquiries too minute to be practicable. The returns of the taxpayer call for exercise of judgments as well for a transcript of the figures on his books. They are subject to possible inaccuracies, almost without number. Salaries of superintendents, figuring as expenses, may have been swollen inordinately, appraisals of plant, of merchandise, of patents, of what not, may be erroneous or even fraught with frauds. These difficulties and dangers bear witness to the misfortune of forcing methods of taxation within a procrustean and rigid formula (emphasis added).[407]

Obviously mindful of the unfavourable state of affairs and in order to achieve "level playing field, the law provides for expenses that are allowable and those not allowable"[408] in the computation of profits of downstream companies. Thus, the allowable or disallowed expenses are applicable to all companies. Yet, the field may still not be level as some companies are wont to prepare two payslips for their employees, for example. However, this action and such other schemes or antics on the part of any company may amount to tax avoidance or evasion. It is now sought to consider the level-playing field provisions of the CITA. It is therefore sought to examine the allowable and disallowable

[406] Per **Pennycuick** in **Odeon Associated Theatres Ltd v. Jones** (1971) 1 W.C.R. at p. 933.
[407] **Steward Dry Goods Co v Lewis** 294 US 550, cited in: Arogundade, op cit.
[408] Ibid.

expenses which determine the assessable profits of a downstream petroleum company in Nigeria.

4.4.1 ***Statutorily Prescribed Allowable Expenses*.** It is not every item of expenses in the audited accounts of a downstream company that will be reckoned with in the computation of the company's tax liability. Accordingly such expenses must meet some standards, which if applied against such expenses will likely remove subjective value judgments of the taxpayer. Thus, expenses allowable and deductible are those that are "wholly, exclusively, necessarily and reasonably"[409] incurred for or in the production of the profits of the downstream company. They include interests, rents and premiums, repairs and maintenance, bad and doubtful debts, contributions to a pension fund, etc. although the CITA provided lists of allowable expenses, it is submitted that each of the expenses must meet the tests of having been incurred wholly, exclusively, necessarily and reasonably in the production of the income. Likewise, "an expense may not be disallowed simply because it is not listed in the section"[410], except of course it is specifically disallowed by the CITA.[411]

Unfortunately, the terms 'wholly', 'exclusively', 'necessarily', and 'reasonably' are not defined either any of the taxing statutes.[412] Secondly, under the PPTA, the word 'reasonably' was not included. As narrowing as the choice of the words show, it has been submitted that strictly speaking,

[409] Section 24 CITA 2004.
[410] Arogundade, op cit, p. 180.
[411] See section 27 CITA 2004.
[412] The PPTA, CITA or PITA.

> *Only expenses of a blatantly extravagant nature or expenses incurred which are wantonly unreasonable and are for the private or selfish benefits of the directors and their associates that can in practice be readily disallowed, because of no common standard as to what is necessary or reasonable (emphasis added).*[413]

Notwithstanding the illuminating submission of the learned author above, an analysis of some decided cases show that there is a guide in deciphering expenses that meet the standards of the law. Thus in the Nigerian case of **Gulf Oil Co Nigeria Ltd v FBIR** (supra) the words 'wholly' is defined to mean 'entirely'; 'exclusively' as meaning 'substantially or even solely'; and 'necessarily' as meaning 'appropriately or inevitably'. Further, **Turner J** stated that in order to ascertain whether an expense was exclusively incurred in the production of the assessable income its effect may be examined.[414]

On the other hand, **Dixon CJ** clarifies on the meaning of the word 'necessarily' when he stated that the operation of the word necessarily is to place a qualification upon the degree of connection between the expense and the activities of the business. In order words, qualification means that the "expenditure must be dictated by the business ends to which it is directed, those ends forming part or being truly incidental to the business".[415] For example, as held in **Moffat v Webb**[416]**,** the possession of land is undoubtedly necessarily incidental to carrying on the business of a grazier, the payment of land tax is a necessary consequence of the possession of land of taxable value. This means that the tax paid on the land is a necessary incident to carrying on the business of grazing. This will also be the case for the business of oil refining or petroleum marketing as in owning and operation of service stations.

[413] Ayua, op cit, p. 179.
[414] **Commissioner of Taxes (New Zealand) v Webber** (1956) 6 ALTR 291.
[415] **Federal Commissioner of Taxation v Snowden & Willson Pty Ltd** (1958) 99 CLR 431.
[416] (1913) 16 CLR 120

Generally due to the fluidity of the business environment the factors which determine whether or not an expense would qualify for deduction are not, and cannot be, cast in concrete. This means that the nature of the business of the company, the circumstances attending to the item of expenditure, the specific environment of the business and other laws regulating the particular business contribute to influence a decision as to whether an item of expenditure is allowable and deductible and vice versa. In other words, the expense would be placed against the exigencies of the business imperatives to see whether it should be incurred. For instance, in the English case of **Morgan (Inspector of Taxes) v Tate & Lyle Ltd**[417] the court allowed an amount spent on propaganda against the Labour Party in the UK as deductible because it was to preserve the assets of the company from seizure and to enable it continue in business to earn profits. Thus, an expense may be treated as meeting the tests for company A, and yet be differently viewed in respect of company B. For example, downstream companies that engage in vigorous social responsibility in the Niger Delta may successfully treat such expenses as deductible.[418]

4.4.2 ***Ministerial Prescribed Allowable Expenses***. The law provides that for the purpose of ascertaining the profits or loss of any company of any period from any source chargeable with tax, there shall be deducted such other deduction as may be prescribed by the Minister by any rule.[419] Accordingly, any prescribed deduction by the minister must be in synchrony with the omnibus ground, that is such deduction must be, exclusively, necessarily and reasonably incurred in the production of those profits. It is submitted that the

[417] (1955) LR 21**; see also Mitchell v B.W. Noble Ltd** (1927) 1 KB 719, where the expenses in getting rid of a director to save the company from scandal was allowed as being wholly and exclusively incurred for the business of the company.
[418] For instance, the case of **Western Soudan Exporters Ltd v FBIR** (1973) CCH/CJ/1/73 12, where it is held that an expense that is customary in a given environment must be recognized for a business to survive in that environment.
[419] Section 24(j) CITA 2004.

exercise of the discretion by the minister must accord with good law, good reason and must be in good faith. That is the minister must be guided by elementary rules of fairness. Thus, where a taxing statute provides that the minister may disallow any expense which he may in his discretion determine to be in excess of what is reasonable or normal for the business carried on by the taxpayer[420], the minister in acting under this provision must produce any facts which informed his opinion. Thus, where the minister failed to produce the ground to support his determination of what was in excessively unreasonable for the business being carried on by company, the Court would allow an appeal against any ministerial decision unsupported as it were..[421]

But, once the discretion is exercised judiciously and in good faith uninfluenced by any extraneous considerations, it appears that courts will not go into the way and manner the discretion was exercised. Thus, **Lord Denning[422]** stated that a clause conferring unfettered discretion is an emergency procedure, which "has to be set in motion quickly, when there is no time for minute analysis of facts or law. The whole process would be made of no effect if the Minister's decision was afterwards to be conned over word by word, letter by letter, to see if he has in any way misdirected himself. That cannot be right". So the minister is only limited in the exercise of his/her discretionary powers by the justiciability of such decision.

4.4.3 ***Allowable Donations*.** Certain categories of donations by companies engaged in downstream operations are allowed as tax deductible expenses,

[420] See section 6(2) Income War Tax Act, 1927.
[421] See **Minister of National Revenue v Wright's Canadian Ropes Ltd** (1947) AC 109.
[422] In **Employment Secretary v. ASLEF (No. 2) (1972) 2 QB 455.**

subject to the conditions specified under the Act.[423] Thus, the donation must be made out of the profits of the downstream company; such donation is limited to ten percent of the total profits of the company; it must be an expenditure of a revenue nature; the beneficiary must fall under the body recognised in the Fifth Schedule of the Act and notwithstanding the latter, the beneficiary must be a public fund, established in Nigeria and having a public character. It would appear that donations to private educational institutions would be outside the ambit of this law, since, strictly speaking, they cannot be said to be of a public character. For instance, private educational institutions are not covered in the intervention initiatives of the Education Tax Fund.

More on allowable donations, it is submitted that the above situation has been dramatically changed by the **Companies Income Tax (Amendment) Act, 2007.** Accordingly, the law provides that there shall be deducted the amount of donation to a university and other tertiary or research institutions for research or any development purpose or as an endowment out of the profits of the period by the company.[424] It is instructive to note that the law does not distinguish between private and public university and tertiary institution. It is therefore submitted that any such donation to a private university will be allowed as tax deductible from the profits of the donor company.

Secondly, the 2007 amendment law provides that any donation made by a downstream petroleum operations company shall be tax deductible whether such a donation is of a revenue or capital nature. This is an improvement over the old law which limited the donation to revenue nature only. However, even

[423] Section 25 CITA 2004.
[424] Section 7 CITA 2007.

this is of limited application. In other words, where the donation is of a capital nature it must be to a university or other tertiary or research institutions, for instance, a polytechnic, or a college of education or a research institution, for example, the Mathematical Research Centre, the National Cereals Research Institute, etc. Thirdly, the new law increased the amount of donation from 10 per cent to 15 per cent of the total profits of the company or 25 per cent of the tax payable by the company in the year of the donation, whichever is the higher amount. This too is of limited application, so that a donation to any other body in the Fifth Schedule other than a university or other tertiary or research institutions will not qualify for deduction under this provision.

4.4.4 ***Disallowable Expenses***. It is not every item of expenses in the audited accounts of a downstream company that will be reckoned with in the computation of the company's tax liability in any given financial year. Accordingly such expenses must meet some standards, which if applied against such expenses will likely remove subjective value judgements on the part of the downstream petroleum operations corporate taxpayer. There are three categories of disallowable expenses under the CITA. Put in another, for any expense to be allowed as tax deductible, it must satisfy one of two tests.

One, where the expense is allowed but it failed to meet the precondition for its allowance or toleration by the FIRS, it will be disallowed as tax deductible. In other words, the expense did not satisfy the test of, or was outside the category of expenses, being 'wholly, exclusively, necessarily and reasonably incurred in the production of the profits[425]' of the downstream operations company. This means that, albeit the expense is allowed under the CITA and

[425] See pp. 149-151 for the meaning of these words, 'wholly', 'exclusively', 'necessarily', and 'reasonably'.

therefore deductible, yet it cannot be so deducted from the profits of the company because the taxing authority, in construing such an expense, cannot find any nexus between the expense and the business activities of the corporate taxpayer, the downstream petroleum operations company.

Second, this is where the expense item has been specifically and expressly disallowed by the CITA.[426] That is, the question of whether the omnibus condition of an expense being 'wholly, exclusively, necessarily and reasonably incurred in the production of the profits', does not, and will not, arise under this second test or condition. Hence, it is immaterial that those expenses were wholly, exclusively, necessarily and reasonably incurred by the taxpayer. This section has an overriding effect: where there is any provision in the CITA which allows certain items of expenditure but is now specifically disallowed by the section, such other sections will no longer have effect. This submission is hinged upon the opening statement of **section 27 of the Act**, to wit 'notwithstanding any other provisions of this Act'. Thus this effectually overrides **sections 24, 25 and 26 of the CITA**, so that if any expenditure is allowed under those sections of the law but latter disallowed under section 27, it is the latter section that will stand. The law provides that, among others, capital repaid or withdrawn and any expenditure of a capital nature is not allowed in ascertaining the profits of any company.

Other disallowable expenses listed by the section include depreciation of any asset, any sum recoverable under an insurance or contract of indemnity, penalty for unlawful act since this cannot be said to have been necessarily incurred, any general reserve, general provision or contingent liability or an

[426] Section 27 CITA 2004.

expense that cannot be ascertained with substantial accuracy, etc. The term 'expenditure of a capital nature' has been a subject of philosophical exposition. It has thus been stated the tax reclassification of expenditure into revenue and capital is the metaphor of the tree and the fruit it bears. Thus,

> the tree is the capital invested and the interest is the fruit the tree bears as the return on the investment. When the harvests are gathered (that is, during the computation of the adjusted profit) what is allowed is the fruit (the interest or rent) and the body of the tree (that is, the capital or rights) is still left to produce more fruits. In the ascertainment of the adjusted profits of any downstream company, the same principle goes into what is allowable, i.e. revenue expenditure or any expenditure of revenue character and what is not allowable, i.e. capital expenditure or any expenditure of capital nature **(emphasis added)**.[427]

Deriving from the above metaphor, it can be said that capital expenditure is normally spent once and for all, while revenue expenditure, being a recurrent decimal, occurs and recurs year in year out. The former is not deductible, being a capital expense, but the latter is deductible since it recurs. In this light, **Lord Cave** illumines that

> when an expenditure is made not only once and for all, but with a view to bringing into existence an asset or advantage for the enduring benefit of a trade, I think there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable, not to revenue, but to capital.[428]

Albeit, there is 'no single, infallible test for settling the vexed question'[429] of what constitutes revenue expenditure as distinct from capital, the courts will reckon with some factors in deciding questions touching upon this issue. That being the case, each case must depend on its particular facts, so that what may have weight in one test of circumstances may have little weight in another. For instance, where a company paid compensation to its agent for the

[427] Arogundade, op cit, p. 183.
[428] **British Insulated and Helsby Cables Ltd v Atherton** (1929) AC 205; 10 TC 155. See also an earlier case of **Vallambrossa Rubber Co Ltd v Farmer** (1910) 5 TC 529.
[429] Per **Lord Macdermott** in **Henry Ferguson (Motors) Ltd v IRC** (1951) NI 115 CA.

termination of agency contract, the court held that it was revenue expenditure, because 'the company was neither enlarging its operations nor improving its goodwill in making the payment'.[430] This means that, although the expense was a one-off item, it could not qualify as a capital expenditure in Lord Cave's dictum in **Atherton's case (supra)**. Examples of expenses of a capital nature within the operations of a downstream company will include acquisition of new leases, preliminary expenses on the formation of a company, pre-production expenses, issues of shares and debentures.[431]

4.5 DETERMINING THE TOTAL PROFITS OF DOWNSTREAM COMPANIES

It has been considered above that the ascertainment of the profits of a downstream company is a function of reckoning with allowable and disallowable expenses. The total profits of a downstream company is the aggregate of all assessable profits from all sources with any additions made less any deductions to be made or allowed under section 31 of the CITA. Such deductions will include capital allowances, ascertained losses, and investment allowance. The specie of deductions, other than those already considered,[432]will now be considered.

4.5.1 **Treatment of Losses**. In computing the total profits of a downstream company during any preceding year of assessment, the law ordains that any losses incurred by the company shall be deductible.[433] This provision is not a blanket cheque for downstream companies to post losses as there are made

[430] **Anglo-Persian Oil Co Ltd v Dale** (1932) 1 KB 124.
[431] Soyode and Kajola, op cit, p.293.
[432] That is, allowable deductions, exempted profits and deductions by ministerial prescription.
[433] Section 31 CITA 2004

subject to conditions. One, the aggregate deduction from the profits must not exceed the amount of the loss – that is, the downstream company is obligated to deduct 'actual', and not manipulated 'book', losses.

Two, the amount deductible is limited to the amount of assessable profit included in the total profits for that year and derived from the source in respect of which the loss was sustained. Thus, the taxpayer with income sources from his profession as a teacher, the rent from his property and the income from his trade, who seeks to set off loss from his trade against the income from other sources, will not be heard. This is because, albeit the amount of assessable income of the trade included in the gross income was nil, no deduction will be made, and the amount of loss will be carried forward, subject to a limitation period of four years, until profits are shown in the particular trade or business.[434]

For example, if **XYZ Downstream Company Ltd** is engaged in petrochemical production, oil refining, transportation of crude by ocean going tankers, and gas utilisation activities. Assuming the company made up its accounts for 2009 assessment, made profits in all areas of its operations (income sources), save gas utilization where it sustained a loss which did not exceed its profit for the year. The rule states that in reckoning with losses sustained, the company can only deduct the loss from the profits derived from its gas utilization operations, and not from the profits made from other sources. In other words, deduction of losses is income-source-dependent, so that the company is not permitted to deduct the loss from its gas utilization operations from the profits derived from petrochemicals production activities. It has been submitted that

[434] Per **Ademola CJ**, in **FBIR v Adenubi** (1963) FSC 442/1961

the rule requiring deduction to be income source dependent are principally to encourage business efficiency and to discourage the continuance of moribund or unproductive businesses at the expense of the Revenue.[435]

Three, the loss can be carried forward and set off against the profits from the same income source subject to a maximum period of four years. Thereafter any unabsorbed losses lapses. However, companies engaged in agricultural trade or business activities are exempted from the four-year limitation period. In other words, they can carry forward their losses *ad infinitum* until they have been completely wiped off.[436] It is submitted that this provision is directed at evasive and avoidance schemes by companies, without which there will unabated perpetuation of losses from its operations.

4.5.2 **Capital Allowances**. Accounting, internal control or management policies of companies differ from company to company. This means that in the treatment of depreciation of assets rates may differ from one company to another. In order to address the inequities which may arise thereby, the law disallows depreciation of assets based on the internal policy of the company.[437] Thus, it is the wisdom of the law to provide a level-playing field for all companies. In order to achieve this, capital allowances are granted to companies and are determinable in accordance with the provisions of the second Schedule to the Act in total disregard to the internal policies of companies.[438] This level-playing field is achieved by the use of the straight line

[435] Ayua, op cit, p. 182.
[436] Section 31(3) CITA 2004.
[437] Section 27(e) CITA 2004.
[438] See sections 31(1) CITA 2004.

method of computing annual allowance is in practice, in which the cost of an asset, less initial allowance, is written off in equal instalments every year.

It is important to note that the grant of capital allowance is not automatic. Rather, they are granted in respect of qualifying expenditure[439] incurred in a basis period with respect to plant, machinery and fixtures, buildings, structures or works of a permanent nature, mines, oil wells, or other sources of mineral deposit of a wasting nature, research and development, furniture and fittings, etc.

1. **TYPES OF CAPITAL ALLOWANCES**.

(a) **Initial Allowance**.[440] Normally granted once, it is allowable in the year of assessment in its basis period for which the asset was first used for the purpose of the trade or business of the downstream company. The rate of initial allowance is as set out in Table I to the Second Schedule. For instance, under the Table I, the rate of initial allowance for qualifying building expenditure is 15 per cent, plant expenditure (excluding furniture and fittings) is 50 per cent, furniture and fittings expenditure is 25 per cent, research and development expenditure is 95 per cent, etc. Paragraph 6(3) of the Second Schedule provides that there shall be allowed a once and for all 95 per cent capital allowance in the first year, **where a company incurs qualifying expenditure for the purchase of plants and machineries for the replacement of the old ones** (emphasis mine). The outstanding five per cent shall be retention as the book value until the final

[439] Qualifying expenditure, in which case it could be qualifying plant expenditure, qualifying building expenditure, qualifying mining expenditure, qualifying research and development expenditure: see Para 1(1), 2nd Sch., CITA 2004.
[440] Paragraph 6, Second Schedule, CITA 2004.

disposal of the asset. In any case, the aggregate capital allowances granted for any asset cannot exceed 95 per cent of the total cost of the asset.

(b) **Annual Allowance**.[441] This is granted additional to the initial allowance for each year of assessment, in its basis period that the asset was used for the purpose of that trade or business carried on by the downstream company. The applicable rate is detailed in Table II. It is possible that an asset may be in use for less than one year. Where this is the case the annual allowance for the assessment year is consequently prorated. The residue of N10 is retained in the accounts for tax purposes pending the disposal of the asset. This last point will not apply to capital expenditure on plant and machineries for replacement of old ones, which requires five per cent to be retained in the books pending disposal. This submission is borne out of the principle of interpretation ***expression unius est exclusio alterius***, that is to express one thing implies the exclusion of the other.

(c) **Investment Allowance**. This is claimed on certain specific assets, and normally once in the first year of use of the asset. Investment allowance is different from other allowances (i.e., initial or annual allowance) because it is not reckoned with when determining the tax written down value of the asset, and it cannot be carried out where it is not utilized in the year in which it is claimed. Thus, a downstream company, keen on tax management strategy, will claim investment allowance ahead of both initial and annual allowances since these can be carried forward.

[441] Paragraph 7, Second Schedule, CITA 2004.

Available investment allowances include 10 per cent investment allowance on plants and machineries in agricultural and manufacturing business; 15 per cent investment allowance on the production machineries of manufacturing companies in so far the machineries have been acquired in replacement of obsolete ones.[442] There is also rural investment allowance, with varying rates and claimable by any downstream company for assets acquired for use in its locations that are at least 20 kilometres away from certain facilities. For instance, where there are no facilities at all, the investment allowance is 100 per cent; where there is no electricity, it is 50 per cent, etc.[443] Further, there is export processing zone allowance, which grants 100 per cent capital allowance to a company which has incurred expenditure in its qualifying building and plant equipment in an approved manufacturing activity in an export processing zone.[444] Once claimed, the export processing zone allowance disentitles a company from claiming investment allowance.

(d) **Balancing Allowance**.[445] This is an allowance granted where qualifying expenditure has been incurred in respect of an asset in use for the purpose of a trade or business carried on by the downstream company. The balancing allowance arises where the asset is disposed of and the proceeds of the disposal are lower than the residual value of the asset. Thus, balancing allowance is the difference between the residual value and the sale value. This difference, called balancing allowance, is deductible against the total profits of the company.

[442] Section 32 CITA 2004
[443] Section 34 CITA 2004
[444] Section 35 CITA 2004.
[445] Paragraph 9, Second Schedule, CITA 2004

For example, if **XYZ Downstream Company Ltd** owns a power generator that was bought at N4.8 million. Meanwhile the book value of the asset is N2.8 million (after reckoning with capital allowances already claimed). If the generator was subsequently sold at N1.2 million, the difference between the proceed of the sale (N1.2 million) and residual value (N2.8 million) is N1.6million. The balancing allowance which will be allowable to the company is N1.6 million and this will be deducted from the total profits of the company. It should be noted that a balancing allowance is only allowable if the asset was in use by the company in the business of downstream operations immediately prior to its disposal. Secondly, it is submitted that if the disposal was not at arm's length, the FIRS may disregard such transaction. In such a case, it will treat it that the asset was disposed of without being sold, so that the amount which the asset would have fetched if sold in the open market or at arm's length transaction, would be dependent on the opinion of the FIRS.[446] It is this amount, based on the opinion of the FIRS that would constitute the balancing allowance. This way the FIRS could check tax avoidance schemes by companies under the balancing allowance provision.

(e) **Balancing Charge**.[447] This is a reverse provision to balancing allowance. Thus, where the value of an asset at disposal is higher than its residual or written-down value, the excess will be reckoned as profit. The asset must be in use immediately prior to its disposal and the charge must not be higher than the total allowances already granted. In other words, the balancing charge is limited by total allowances already granted. For

[446] See Paragraph 13 Second Schedule CITA 2004; section 22 CITA 2004.
[447] Paragraph 10 Second Schedule CITA 2004

instance, where **XYZ Downstream Company Ltd** acquires equipment for its fluid catalytic cracking unit (FCCU) at N3 million, and has already been granted allowances to the tune of N2.5 million, leaving the asset with a residue of N500,000. If the equipment is subsequently sold at N3.7 million, the balancing charge will be the difference between the proceeds of N3.7 million and N500,000, which is N3.2 million. The law provides that the balancing charge must not exceed the value of allowances already granted, so that the balancing charge to be made on the company is N2.5 million. It is hardly that companies operating in the downstream petroleum sector will disclose such cases where the disposal of an asset exceeds its book value. It is submitted that the only case where the FIRS will bring this provision to bear on the practical plane is where a transaction is artificial or between the company and a fictitious person or an entity. In such a case, if the FIRS forms an opinion that the open market value of the asset is far in excess of the disposal value and the residual value, then the issue of balancing charge will arise. Therefore, practically speaking, it is submitted that the operation or application of provision is of little relevance.

2. LIMITATIONS ON CAPITAL ALLOWANCES.

There may in any given year be a situation where capital allowances to a company may outstrip its assessable profits for the year of assessment. In order to ensure that the government is not deprived of needed revenue for fiscal policy and economic development, a ceiling is placed on the amount of capital allowances which a company can claim in any given year of assessment. Thus, the amount of capital allowances to be deducted from assessable profits shall not exceed $66^{2}/_{3}$ per cent of such assessable profits of a downstream

company.[448] Were it not so, it is submitted, the assessable profits of downstream companies will be wiped off by phoney capital allowance claims.

Also, where a downstream company incurs qualifying capital expenditure for purchase of plants and machineries in replacement of old ones, a once and for all allowance of 95 per cent is provided. This leaves five per cent as retention pending the disposal of the asset.[449] Further, the maximum claim that can be made for the aggregate capital allowances and investment tax allowances is 95 per cent of the total cost of the asset. However, the limitation on capital allowances that can be deducted from the assessable profits of downstream companies in any year of assessment does not apply to any company engaged in the agro-allied industry or manufacturing.

3. **RATES OF CAPITAL ALLOWANCES**.

As noted earlier, the rates of capital allowances (whether initial, or annual, allowance) are as contained in Second Schedule. The National Council of Ministers has powers to vary the rates of the allowances. Where such changes are made, they are normally published in the official gazette. The rates of capital allowances as at 30/4/2005[450] are tabulated below:

[448] Paragraph 24(7) Second Schedule CITA 2004.
[449] See n. 420, p. 161 above.
[450] Arogundade, op cit, p. 200.

S/N	TYPE OF ASSET	INVESTMENT ALLOWANCE RATE (%)	INITIAL ALLOWANCE RATE (%)	ANNUAL ALLOWANCE RATE (%)
1	Building (industrial and non-industrial)		15	10
2	Mining		95	Nil
3	Plant: agricultural production		95	Nil
4	Plant: others		50	25
5	Furniture and fittings		25	20
6	Motor vehicle: public transportation		95	Nil
7	Motor vehicle: others		50	25
8	Plantation equipment		95	Nil
9	Housing estate		50	25
10	Ranching and plantation		30	50
11	Research and development		95	Nil

SOURCE: ADAPTED FROM AROGUNDADE, 2005

4. BASIS PERIOD FOR CAPITAL ALLOWANCES.

All along in the discussion of capital allowances, reference has been made to basis period. It is important to determine the basis period in order to have correct computation of capital allowance to be claimed by the company. One of three scenarios[451] may be the case in the determination of the basis period for capital allowance purposes:

(a) The basis period for the assessable profit may be exactly equal to the basis period for capital allowance. Under this scenario, the computation of the capital allowance will present no difficulties.

(b) There may be a scenario in which two basis periods overlap or coincide. Where they coincide, or overlap, and a qualifying capital expenditure is acquired on a date that falls into more than one basis period then there is cessation of business. Thus, the asset so acquired would be allocated to the earlier tax year, since where the two basis

[451] Paragraph 1(1) Second Schedule CITA 2004; section 29 CITA 2004.

periods overlap or coincide, a date will occur in more than one basis period. According to M.T. Abdulrazaq, "this will mostly occur under the commencement rule and sometimes where there is a change in the accounting date".[452]

(c) The third scenario is a case where there is gap between two basis periods. Where this is the case, it means that a qualifying capital expenditure may be acquired on a date that fell outside any basis period. This scenario will normally arise under the cessation rule and at times where there is a change in accounting date. As a general rule, where a qualifying capital expenditure is acquired on a date that fell outside any basis period and there is a change in the accounting year end of the company, the qualifying capital expenditure would be allocated to the latter tax year. On the other hand, where the gap arises where there is cessation of business, such an asset would be allocated to the earlier tax year.[453]

4.6 INVESMTENT TAX CREDIT

Investment tax credit (ITC) is a set off against the tax payable, unlike investment allowance which is deductible from the assessable profit of downstream company. The CITA ordains that where a company has incurred expenditure for the replacement of an obsolete plant and machinery, there shall be allowed to that company, 15% investment tax credit.[454] It has been submitted that this provision contradicts the proviso to paragraph 6(3) of the Second Schedule to the CITA, which states that the aggregate allowances granted in respect of any asset and section 30

[452] Abdulrazaq, M.T., **"Legal Mechanism for Corporate Tax Relief"**, Juriscope, vol 1, 2nd Edn., (2001) p. 114
[453] Abulrazaq, op cit, p. 115.
[454] Section 41 CITA 2004.

CITA 1990 shall not exceed 95% of the total cost of the asset. Accordingly, this contradictory provision has made the provision inoperative in practice and explains the administrative substitution of s. 28 for section 30 in the proviso.[455]

It is submitted, with due respect to the author who obviously is writing from practical experience as a former director of the FIRS, that the law is muddled up both in construction and application. This is because, capital allowance in the nature of initial or annual allowance, capital allowance in the nature of investment allowance and investment credit are not the same and do not have similar tax effects. Thus, initial allowance and annual capital allowances can be carried forward to the next year of assessment, if due to the requirements of the law they cannot be claimed within the year in which they became claimable. On the other hand, investment allowance is claimable once in the first year in which it was acquired and used for the business carried on by the downstream corporate taxpayer. Investment tax credit is a credit not an allowance. This is why it is set off against tax payable as against assessable profits. It is allowed and claimable once, and is meant to encourage conscious industrial renewal so that the company continues to operate optimally.

The resort to section 28 as an answer to the misguided application of the law cannot help matters either. This is because **section 28 CITA** makes provisions for an investment allowance of 25 per cent for expenditure incurred by a company on a new asset as a replacement of an asset damaged or destroyed during the Civil War. It also provides for investment allowance of 10 per cent for qualifying expenditure incurred on plant and equipment for agricultural production other than in marketing and processing. The investment allowances are additional to initial and annual allowances allowable on the assets. It is therefore difficult to see how, following the

[455] Arogundade, op cit, p. 203

construction of the section, the section 28 could be applied hand in hand with paragraph 6(3) of the Second Schedule without offending the threshold provision that the aggregate capital allowance on any asset under the Schedule must not exceed 95 per cent.

The only practicable and legally tenable position, it is submitted, is that the provisions are not after all contradictory, though so it may appear to ordinary minds. Since they are not contradictory, therefore, it is submitted that the taxpayer is provided with strong incentives to whittle his tax obligations by first claiming the investment allowance, and carrying forward the initial allowance in respect of that asset. It should be recalled that there is a ceiling of $66^{2}/_{3}$ per cent as the maximum capital allowance that can be deducted from the assessable profits of a downstream company in any given year. This means that the outstanding would normally be carried over to the assessment year, provided that within the outstanding amount investment allowance of a previous year's assessment is included.

4.7 INCENTIVES TO DOWNSTREAM COMPANIES UNDER CITA 2004

Under CITA 2004 gas utilization has been classified as downstream operations. It is defined as the marketing and distribution of natural gas for commercial purposes and includes power plant, liquefied natural gas, gas to liquid plant, fertilizer plant, gas transmission and distribution pipelines.[456] In line with this definition, a company engaged in downstream gas utilization operations shall be granted an initial tax-free period of three years which may, subject to the satisfactory performance of the business, be renewed for an additional period of two years. This means that the

[456] Section 39(3) CITA 2004.

company is subrogated in the position of a pioneer company status that equally tax holidays of up to a maximum of five years.[457]

Recognizing that the company may opt for other options, the law puts it to election. Thus, instead of appropriating the provision as to tax free period up to a maximum period of five years, the company may claim an additional investment allowance of 35 per cent. This is taken to start on the day the company commences production as certified by the Ministry of Petroleum Resources.[458] It is doubtful if this incentive is sufficiently attractive enough to warrant its embrace by the downstream operator. This is because the company is prevented from also claiming further incentive, discussed below, under section 39(1)(c)(ii) of the CITA. However, this does not blur the wisdom. Some downstream operators, desirous of recouping at the earliest their investment, may opt for this alternative. Either way, the provisions are made to encourage gas utilization in the country in line with the government's gas master plan.

In addition, where a company opts for the tax-free period incentive, it is entitled to an additional investment allowance of 15 per cent. This 15 per cent can only be claimable after the expiration of the tax free period. However, whether a company opts for tax free period incentive or the 35 per cent investment allowance incentive, both companies are entitled to accelerated annual capital allowance of 90 per cent with 10 per cent retention for investment in plant and machinery.

Generally, all gas utilization companies are entitled to the generous incentive of tax free dividends during the tax free period, but where the investment for the business was in foreign currency or the introduction of imported plant and machinery during

[457] Section 39(1)(a)
[458] Section 39(2) CITA 2004.

the tax free period was not less than 30 per cent of the equity share capital of the company. Additionally the interest payable on any loan obtained with the prior approval of the Minister for a gas project shall be tax deductible. It is submitted that these incentives will claimed in addition to the incentive provided for every company under **section 42 CITA 2004**. The section grants relief to every Nigerian company at a rate equal to the full rate of tax upon the first N6,000 of the total profits of such a company. In other words, a tax bonus of N1,800 (30% of N6,000) will be enjoyed by the company.

Under the newly enacted **Nigerian Oil and Gas Industry Content Development Act 2010,** it is provided that appropriate framework and tax incentives shall be given to foreign and indigenous companies which establish facilities, factories, production units and other operations in Nigeria for purposes of carrying out production, manufacturing or for providing services and goods otherwise imported into Nigeria[459]. It is submitted that this incentives provision is nebulous and vague. The target items are those equipment which are utilised in the oil and gas industry, which presently are wholly imported into the country. They will include flow measurement systems, electronic counting machines, valves, mechanical seals, molecular sieves, etc. The establishment of such industries or manufacturing plants are extremely capital intensive and will require concrete and firm assurances before any foreign or even indigenous company can venture into that activity. Thus, the way in which the incentives provision is couched casts doubt over the clear intentions of the government to encourage and stimulate local manufacturing of such items.

The question may be asked, how effective have these incentives proven. Has the country witnessed massive and substantial investments in this area of downstream

[459] See section 48 of the Act.

operations of the petroleum industry? It is not likely. Agreeing in this light, it has been stated that "tax incentives are not the answer to Nigeria's quest for investment. Rather, the factors that act as disincentives need to be addressed".[460] These factors are security, convertibility of local currency, political stability and markets.

4.8 RATE OF INCOME TAX OF DOWNSTREAM COMPANIES

There is inverse relationship between the capital allowances and the tax payable. Hence, the more generous the capital allowances policy, the lower the revenue yield. Likewise, there is a nexus between the tax rate and the tax revenue – hence the higher the tax rate, the higher the revenue yield.[461] Without recoiling to historical antecedents, the current corporate tax rate which became effective since 1996 is 30 per cent. However, the National Council of Ministers has powers to vary, by order, the tax rate for any assessment year.[462] This provision makes for administrative convenience, so that amendments to the rates either way need not go to the National Assembly before they become effective. They become effective and enforceable once they have been approved by the National Council of Ministers and duly gazetted. However, it should be noted that the power granted to the Council is not power to introduce new taxes. Doing the latter would be ultra vires the Council, an illegality.

There is a provision for payment of minimum of tax by companies, and this is irrespective of the provision as to the rate of tax.[463] Consequently, notwithstanding any other provisions in this Act where in any year of assessment the ascertainment of total assessable profits from all sources of a company results in a loss, or where a company's ascertained total profits results in no tax payable or tax payable which is

[460] Arogundade, op cit, p. 207.
[461] Arogundade, op cit, p. 206
[462] Section 100 CITA 2004.
[463] Section 40 CITA 2004.

less than the minimum tax, there shall be levied and paid by the company the prescribed minimum tax.[464] For example, if the turnover of a downstream operations company is N500,000 or below and the company has been in business for at least four calendar years, then the minimum tax payable by it shall be 0.5 per cent of gross profit; or 0.5 per cent of net assets; or 0.25 per cent of paid-up capital; or 0.25 per cent of turnover of the company for the year, whichever is higher. By this provision, the company is compelled to remit tax in any year of assessment provided it is in business. The company cannot be heard to complain that in its books it posted loss for the year of assessment.

4.9 RETURNS FILING BY DOWNSTREAM COMPANIES

Every downstream operations company whether it is granted exemption from incorporation or not shall, whether under the Act it is liable to pay tax or not, for a year of assessment[465], with or without notice from the FIRS, file a self assessment return with the FIRS in the prescribed form once a year.[466] The return shall contain, among others, the audited accounts, tax and capital allowance computation for the year of assessment and a true and correct statement in writing containing the amount of profit from each and every source computed, duly completed self-assessment form attested to by a director or secretary of the company and such attestation shall contain a statement of declaration that it is a true and correct statement of the amount of its profits, and evidence of payment of the whole or part of the tax due into

[464] Section 33 CITA 2004.
[465] See Chapter Five, infra.
[466] Section 13 CITA 2007; section 55 CITA LFN 2004.

a bank designated for the collection of the tax. Notwithstanding, the FIRS has powers under the law to call for further returns as it thinks necessary.[467]

The returns shall normally be made not more than six months after the end of the accounting year for a downstream company that has been in business for more than 18 months; and within 18 months from the date of its incorporation or not later than six months after the end of its accounting period whichever is earlier for a newly incorporated downstream operations company.[468] However, the FIRS, on the application of a downstream company may grant extension of time for making returns, provided that the application was made before the expiration of time stipulated for making the returns and the company shows good cause for its inability to comply with the provisions of the law.[469] Where a downstream company is out of time in making the return and did not apply for extension of the time before its expiration, there is a penalty of N25,000 in the first month in which the failure occurs and N5,000 for each subsequent month in which the failure continues.[470]

The duty to procure compliance and to ensure that CITA as a fiscal law relating to downstream operations is thrust upon the Federal Inland Revenue Service.[471] In other words, the efficacy of the fiscal law is only as good and effective as the administration and enforcement machinery in place. In this light, the next chapter will consider administration and enforcement of fiscal laws relating to petroleum operations in Nigeria.

[467] Section 58 CITA 2004.
[468] Section 13(2) CITA 2007.
[469] Section 59 CITA 2004.
[470] Section 13(3) CITA 2004.
[471] See Federal Inland Revenue Service (Establishment) Act 2007

CHAPTER FIVE

ADMINISTRATION AND ENFORCEMENT OF THE FISCAL LAWS RELATING TO PETROLEUM OPERATIONS IN NIGERIA

5.0 INTRODUCTION

When the Federal Inland Revenue Service (Establishment) Act, 2007 was enacted, the machinery for the administration and enforcement of the fiscal laws relating to petroleum operations in Nigeria was given a boost. Accordingly, in order to give 'teeth' to the enforcement of the fiscal laws relating to petroleum operations in Nigeria, the Federal Inland Revenue Service (hereafter called the 'FIRS') was established and charged with powers of assessment, collection and accounting for revenues accruable to the government of Nigeria from petroleum operations.

Following this paradigm, Part I of the CITA was repealed.[472] The repeal of that Part is understandable, because that is the part that established the predecessor body to the FIRS that is the Federal Board of Inland Revenue. However, apparently out of legislative inadvertence, Part II of the PPTA was not repealed. That Part of the enactment states that the due administration of the PPTA shall be under the care and management of the Board (now, FIRS).[473] But there is o cause for alarm, and no purpose is served dancing around technicalities. This is because the rule of interpretation states that a reference in an enactment to another enactment shall, if the other enactment has been amended be construed as a reference to the other enactment as amended.[474] Thus wherever 'Board' appears in PPTA it means 'FIRS'.

[472] Section 62 FIRS Act 2007.
[473] See section 3 PPTA.
[474] See generally section 4(1) and (2) Interpretation Act, CAP I23 LFN 2004.

5.1 FEDERAL INLAND REVENUE SERVICE

The FIRS was established with the object of controlling and administering the different taxes and laws specified in the First Schedule or other laws made or to be made, from time to time by the National Assembly and to account for all taxes collected.[475] The laws specified in the First Schedule for which the FIRS has power to administer are CITA, PPTA, Personal Income Tax Act, etc.[476]

In order to realise the above object, the FIRS is seized with some statutory functions, including to assess companies chargeable with tax; to assess, collect and account and enforce payment of taxes as may be due; to adopt measures to identify, trace, freeze, confiscate or seize proceeds derived from tax fraud or evasion; and to carry out such other activities as are necessary or expedient for the full discharge of all or any of the functions under the Act.[477] This Chapter will briefly consider the core functions of assessment, collection and enforcement (under this the powers of the FIRS to impose penalty shall be considered as well as the appeal process in case of objection) of the fiscal laws relating to petroleum operations in Nigeria.

Meanwhile, there is Executive Chairman, who must have cognate experience and skills in accountancy, economics, taxation, law and related fields. as the chief executive officer of the FIRS.[478] He or she is supported by Secretary and other staff of the FIRS.[479] The activities of the FIRS is overseen and supervised by the Management Board, known as the Federal Inland Revenue Service Board.[480] There is the Technical

[475] Section 2 FIRS Act 2007.
[476] See, section 25 FIRS Act, 2007.
[477] See, section 8(1)(a)-(t) FIRS Act, 2007;
[478] Section 11 FIRS Act, 2007.
[479] Section 12 FIRS Act, 2007.
[480] Section 3 FIRS Act, 2007.

Committee of the Board headed by the Executive Chairman with all the directors and heads of departments of the FIRS, etc as members. Its role is mainly professional.[481]

Finally, it must be noted that the minister[482] of finance has general supervisory powers over the FIRS and may give directives of a general nature or generally relating to matters of policy with regards to the exercise of its functions.[483] In the administration of the PPTA, the FIRS is equally subject to the authority, direction and control of the minister.[484] However, the minister does not have the power to give any direction, order or instruction as regards any particular company with the effect of requiring the FIRS "to raise an additional assessment upon such company or to increase or decrease any assessment made or to be made or any penalty imposed or to be imposed upon or any relief given or to be given or to defer the collection of any tax, penalty or judgment debt due by such company".[485] The effect of this provision is simply that no company should be advantaged or disadvantaged on account of any direction or order or instructions from the minister. It is thus submitted that such an direction or order instruction will be ultra vires the minister and the FIRS is not bound to obey for that will amount to illegality if duly executed by the FIRS.

5.2 ASSESSMENT FUNCTION OF THE FIRS

Under the law, there are basically two main types of assessment: taxpayer assessment (more generally known as self assessment)[486] and government (FIRS) assessment (which may be based on the returns and audited accounts filed by the company or where the company failed to file a return or the FIRS rejects the returns as filed by the

[481] Sections 9 and 10 FIRS Act, 2007.
[482] Section 69 FIRS Act 2007.
[483] Section 60 FIRS Act 2007.
[484] Section 3(1)(f) PPTA 2004; Article 440(6) PIB 2008.
[485] See proviso to section 3(1)(f) PPTA 2004; Article 440(7) PIB 2008.
[486] Section 13 CITA 2007; section 55 CITA 2004

company based on its best of judgment).[487] Principally, a company in the downstream sector either makes a return and files same with self assessment or the FIRS makes the assessment on the basis of the return filed by the company.[488] However, it seems that self assessment is discreetly compulsory for all downstream companies.[489]

As regards upstream companies, the duty to make assessment lies with the FIRS[490], which assessment shall derive from the accounts and particulars[491] together with returns filed with the FIRS not later than two months after the commencement of each accounting period.[492] This culture of government assessment under the PPTA survived in the Petroleum Industry Bill 2008. Accordingly the FIRS shall proceed to assess every company in the upstream operations sector with the tax for any accounting period of the company as soon as may be after the expiration of the time[493] allowed to such company for the delivery of the accounts and particulars.[494] The FIRS is not bound to accept the delivered accounts and particulars for any accounting period of the company[495], in which case the FIRS may estimate the amount of the tax payable by the company and make assessment accordingly.[496] This simply means that if the FIRS accepts the accounts and particulars as delivered by the company it will proceed to make assessment based on the submission.[497]

5.2.1 SELF ASSESSMENT. This was first introduced in Nigeria in 1991,[498] and subsequently entrenched in 1996.[499] It is retained in the laws of the Federation 2004

[487] Section 65 CITA 2004.
[488] See for self assessment, section 13 CITA 2007; and for government assessment, section 65 CITA 2004.
[489] See section 13 CITA 2007.
[490] Section 35 PPTA 2004.
[491] Section 30 PPTA 2004.
[492] Section 33 PPTA 2004.
[493] See articles 461, 463, 464 and465 PIB 2008.
[494] Article 468(1) PIB 2008.
[495] Article 468(2)(b) PIB 2008.
[496] Article 468(3) PIB 2008.
[497] Article 468(2)(a) PIB 2008.
[498] Finance (Miscellaneous Taxation Provisions) Decree 1991; FIRS Circular No. IR. 5123/C/Vol. 23/157 of 30/9/1991.

edition.[500] However, the subject of self assessment provisions under the CITA has attracted scathing but meritorious criticisms from Arogundade.[501] The crux of the author's critique is that self assessment under CITA 1990 and CITA 2004 was hazy in its legislative flavour and operational outlook. This is because self assessment[502] is only actuated when the FIRS calls for further returns[503] or when a company applies for extension of time[504] within which to make to file a return pursuant to a request from the FIRS[505] or to file its audited accounts and returns,[506] Thus, when a company makes a return under the law, it is not expected to self-assess.[507] Arogundade insists,

> *What section 53 (CITA 2004) provides for as trigger for filing self assessment is where fuller and further information or extension of time for filing returns is required. (Meaning that) if the Board (FIRS) is satisfied with the returns filed under either sections 52(1) or 55, the need for self assessment filing would not even arise. It is only when the Board has validation problems or the taxpayer requests for extension of time that,,, it can compel self assessment returns ... The overall effect of either the 1990 Act or the 2004 Act is to downgrade self assessment to the statutes of a supplementary measure for the traditional assessment system (emphasis added).*[508]

As if to take heed as regards the observations of the author above, the CITA 2007 revolutionised self assessment filing and diametrically changed its operational and legislative complexion. Accordingly, the self assessment provision under CITA 2004[509] was amended. Categorically and removing every shade of ambiguity, it provides that every company shall file with the FIRS, with or without notice from the Service, a self assessment return in the prescribed form at least once a year, and it

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[499] See section 6 Finance (Miscellaneous Taxation Provisions) Decree Nos. 30 and 32, 1996.
[500] See sections 52, 53 and 55 CITA 2004.
[501] Op cit, Arogundade, pp. 311-320.
[502] Section 53 CITA 2004
[503] Section 58 CITA 2004
[504] Section 59 CITA 2004
[505] Section 52(1) CITA 2004.
[506] Section 55(3) CITA 2004.
[507] Section 55(1) CITA 2004.
[508] Op cit, Arogundade, pp. 312-313.
[509] Section 55 CITA 2004; section 41 CITA 1990.

shall be supported by evidence of payment of the whole or part of the tax due into a bank designated for the collection of the tax. [510]

It is hereby submitted that self assessment is apparently not, but discreetly, compulsory under the Act. This is because the Amending Act did not provide for punishment for failure to file a self assessment. It provided penalty where any company makes default in filing returns within the time specified. However, a company that fails to make self assessment will automatically fall in breach of the law. Secondly, where a company fails to make self assessment at all, it is bound to file returns, upon a notice, with the FIRS in the prescribed form.[511] Previously, there was a filing bonus of one per cent of tax payable, and payment of tax by instalment to encourage self assessment.[512] However, the one per cent bonus has been abrogated;[513] while payment by instalment is still allowed.[514]

5.2.2 GOVERNMENT (FIRS) ASSESSMENT. As noted above, self assessment did not totally replace government assessment. This is because the CITA 2007 left section 65 CITA 2004 and section 52 CITA 2004 intact. The wisdom behind this is understandable, because there will always be non-filers, late-filers and stop-filers. Under this type of assessment, the taxpayer is not liable to pay tax unless and until the FIRS has served on it the notice of assessment, based on the return filed by the taxpayer. Under the government assessment, notice is a condition for tax liability and represents one of the core principles of income taxation. Until there is such

[510] Section 13 CITA 2007.
[511] Section 52(1) CITA 2004.
[512] Section 56 CITA 2004.
[513] Section 14 CITA 2007.
[514] Section 13 CITA 2007.

notification[515], no liability will attach to the taxpayer. In other words, the assessment derives its validity only when it is served on the taxpayer.[516]

Secondly, the assessment function of FIRS arises where a company fails to deliver a return. In such a case, the FIRS has power to use best of judgement to determine the amount of the total profits of the company and make assessment accordingly.[517] In doing this, the FIRS may need to obtain full information in respect of the profits or income of the company and is thereby empowered to require such company to complete and deliver to the FIRS any return that will yield such full information.[518] This power includes requiring the company to produce its books or documents for examination.[519] Failure to comply with the request of the FIRS attracts a fine up to 100% of the amount of the tax liability.[520]

Thirdly, the FIRS has power to make additional assessment[521] upon any company, consequent upon the discovery of new facts. To do discharge this aspect of the assessment function effectively, the FIRS can request the company to deliver to it fuller or further returns within a reasonable time,[522] although upon request, the FIRS may grant extension of time within which to comply with its request for further returns.[523] This function is unfettered even though it will mean reopening an assessment that has become final and conclusive.[524] Although this is not to suppose that it is the same as stating that an assessment that was validly raised cannot be reopened once it becomes final and conclusive. An assessment is said to be final and

[515] Section 68 CITA 2004; Section 38 PPTA 2004; Article 472 PIB 2008.
[516] **Joseph Rezcallah & Sons v FBIR** (1962) 1 All NLR 1; **FBIR v West African Pictures Ltd** (1974) 1 FRCR 40
[517] Section 65 CITA 2004.
[518] Section 26(1) FIRS Act 2007; section 17 CITA 2007; section 32(1) PPTA 2004; Article 464 PIB 2008.
[519] Section 26(1)(c) FIRS Act 2007.
[520] Section 26(4) FIRS Act 2007.
[521] Section 66 CITA 2004; section 36 PPTA 2004; Article 470 PIB 2008.
[522] Section 27(1) FIRS Act 2007; section 58 CITA 2004; section 31 PPTA 2004; Article 463 PIB 2008.
[523] Section 26(5) FIRS Act 2007.
[524] **Western Soudan Exporters Ltd v FBIR** (1973) CCH CJ/1/73 12

conclusive if it has not been objected to, or appealed against with respect to the amount of the chargeable income but not with respect to other matters the validity of which can always be looked into by the court except where it is restricted by the Act.[525] However, it must be noted that additional assessment is time-bound.[526] That is additional assessment made out of time, will be statute barred.[527]

However, it must be pointed out that the taxpayer has right of objection against any assessment made on it by the FIRS. With the repeal of Part XI of CITA 2004 by CITA 2007, appeals against any assessment or demand notice by the FIRS shall now be as provided under section 59 FIRS Act 2007 and Fifth Schedule of the Act[528]. As regards the PPTA the situation, it is submitted, is the same, although Part VIII vests appeal against the decision of the FIRS on Appeal Commissioners and then to the Federal High Court. On the principle of interpretation outlined earlier[529], it is submitted that the appeal process against the assessment of the FIRS under the PPTA shall be as provided under the FIRS Act, *mutatis mutandis*. In case of any objection, the burden rests on the applicant to show that an assessment complained of is excessive.[530]

It is submitted from the above discussion that the assessment function as an ambit of administrative tool for ensuring the efficacy of fiscal laws relating to the petroleum industry is thrust upon the taxpayer through the mechanism of self assessment and superintended by the FIRS; and on the FIRS through the mechanism of original

[525] Rezcallah's case (supra).
[526] Section 36 PPTA 2004; section 66 CITA 2004. The limitation period is six years.
[527] **Gulf Oil Co (Nig) Ltd v FBIR** (1985) FHCLR 1.
[528] Section 18 CITA 2007.
[529] See above, n. 455, p. 178.
[530] **FBIR v Diab A. Nasr** (1964) All NLR 408.

assessment, best of judgment assessment and additional assessments. Additional safeguards have been provided by bringing the banks into the equation[531].

5.3 COLLECTION PROCEDURE[532]

Under the self assessment the company which is applicable to downstream companies only, the company is expected to show evidence of payment of whole or part of the assessed tax. Accordingly, self assessment shall be made not later than six months after the end of the accounting year that is not later than 30th June.[533] As noted earlier, there is penalty for late filing and payment of self assessment under the law. Thus, a company in the downstream section which fails to pay latest 30th June of the accounting year shall be liable to pay late filing fee of N25,000 in the first month in which the failure occurs and N5,000 for each subsequent month in which the failure continues.[534] The advantage of self assessment is that there is no room for argument over the assessed tax; but this does not preclude the right of the FIRS to call for further and fuller returns, where new facts emerge. In other words, as regards the company making the self assessment it is final and conclusive since it would have paid either partly or wholly the self assessed tax.

However, under the FIRS assessment, payment shall be made by the company in lump sum and once not later than two months after the service of notice.[535] The disadvantage of FIRS assessment is that it is open to objection. Thus FIRS assessment cannot be said to be final and conclusive when there is objection.[536] So where the company assessed to tax by the FIRS objects within the time specified for raising such objection, the collection of the tax "shall remain in abeyance until such objection or

[531] See infra, p. 198.
[532] See above, n. 311, p. 127.
[533] Section 13 CITA 2007.
[534] Section 13 CITA 2007.
[535] Section 77(2) CITA 2004.
[536] See for instance, Article 476(1) PIB 2008.

appeal is determined".[537] After the determination, the FIRS shall now serve the company a notice of the tax payable as so determined and the tax shall be payable within one month of the date of service of such notice upon the company.

Where there is no objection, the assessment is final and conclusive. However, a company cannot, under the disguise of objection to an assessment, be allowed to fish for skirmishes. Consequently, an assessment shall not be impeached or affected by reason of a mistake as to the name of the company liable to tax, or the description of any profits or amount of tax charged or by reason of any variance between the assessment and the notice.[538] However, it must be noted also that there is penalty for any assessment not paid on the due date, which is a sum equal to 10 percent of the amount the tax payable.[539] This provision sidesteps the earlier provision which provided for a non-cumulative 10 percent per annum of the amount of tax payable.[540]

5.4 **POWERS IN AID OF ENFORCEMENT**

To enhance administrative efficiency, the law made provisions for mechanisms which will stimulate efficiency of assessment and effectiveness of collection:

5.4.1 *Customer Account Information*. In order to help the FIRS in procuring accurate assessment of downstream and upstream companies, it has wide powers to call for further returns for the purpose of determining the true amount of taxable profit of any company in any fiscal year[541]. Additionally and for the first time in the tax history of Nigeria, every bank must prepare, upon demand by the FIRS, quarterly returns specifying the name and address of all

[537] Op cit, Soyode and Kajola, p. 52.
[538] Section 70(2) CITA 2004; section 39(2) PPTA 2004; Article 473(2) PIB 2008.
[539] Section 32(1) FIRS Act 2007.
[540] Section 85(1)(a) CITA 2004. Arogundade submits it is 10% for every year of default and it is non-cummulative.
[541] Section 26 FIRS Act 2007.

customers of the bank of all companies (downstream and upstream companies inclusive) whose transactions involve the sum of N10 million and above[542]. It is equally mandatory upon all banks to oblige the FIRS with the returns of the particulars its new customers (whether personal or corporate) not later than the seventh day of the succeeding month[543].

The information required above will indicate the name, address and particulars of the transaction from N10 million and above. It does not require the bank to provide any further or additional information about the customer, for instance showing whether the customer is indebted to the bank or the credit or debit balance of the customer[544]. This is understandable, because of the duty of confidentiality which the bank owes to its customers. However, it is an offence for any bank to refuse to comply with the request of the FIRS and it attracts a fine not exceeding N500,000. This penalty is paltry, especially when we consider the profile of downstream and upstream companies in the petroleum industry. This means that the companies could afford to encourage the banks to disobey the request of the FIRS while they bear the liability, which is just a drop in the ocean as far as their financial base are concerned.

It is equally submitted that the principal purpose of this provision is to enable the FIRS track the activities of companies so that the veracity of the returns filed by the companies, pursuant to self-assessment, can be subjected to objective scrutiny. Secondly, the provision enables the FIRS to keep tab, and maintain real time database, of taxable persons (including companies) in Nigeria. Ultimately, it is a statutory device to enhance the accruable revenue to

[542] Section 28(1)(b) FIRS Act 2007
[543] Section 28(1)(c) FIRS Act 2007.
[544] Section 28 FIRS Act 2007, see the proviso thereof.

national treasury. However, it is submitted that its effectiveness is dependent, largely, on implementation by the FIRS.

5.4.2 *Right of access*. It is not impossible that the FIRS in going about its statutory duties may meet resistance by, or opposition from, the companies. For instance, it may call for further returns[545], and the call is ignored, disregarded or rebuffed. It may make a demand on the bank pursuant to its powers under Act[546], and the bank prefers fine to obliging the customer details[547], especially where the bank is encouraged by the customer to disregard, disobey or discountenance the demand, since, as observed above, the deterrent potential of the penalty for non-compliance is much to be doubted. Where this happens, tax assessment and collection becomes hampered, and thus revenue to the government in endangered.

Cognizance of the above case happening, the FIRS is empowered to have free access to all lands, buildings, places books and documents, whether stored in electronic media or any other form, in the custody or under the control of a public officer, institution or any other person[548], for the purpose of collecting any tax under either the PPTA or the CITA[549]. This power of access includes power to take all reasonable steps to preserve, and prevent the destruction, of the books or documents[550]. In the case of premises, the occupier has a duty to provide to the FIRS all reasonable facilities and assistance to ensure that access is gained to the premises, in so far as the consent of the occupier of a

[545] Section 26 FIRS Act 2007.
[546] Section 28 FIRSA Act 2007.
[547] Section 28(3) FIRS Act 2007.
[548] Any other person will include companies, whether in the downstream or upstream petroleum sector.
[549] Section 29(1) FIRS Act 2007.
[550] Section 29(2)-(3) FIRS Act 2007 and section 30 FIRS Act 2007.

private dwelling must be first had and obtained[551] or formal authorisation obtained for the purpose of entry into a private dwelling[552].

The formal authorisation is in the nature of warrant, since it is issuable by judicial officer on the application of the FIRS. The warrant to enter into any premises must be in the prescribed form[553]; it must be directed to a named officer of the FIRS; it is valid for three months from the date of issue; it must state its period of validity; and it is renewable on application[554]. It is submitted that this mechanism is a general purpose instrument directed at first enforcing tax payment by public institutions and second, at private tax payers, companies inclusive. Secondly, it is submitted that enforcement of this power is dependent upon many factors, some of which include the willingness of the government in power to allow the FIRS undertake its duties without interference, the calibre and personality of the leadership of the FIRS, etc. Either way it will have a telling effect on the revenue of the government.

5.4.3 Distraint Powers[555]. In order to enforce payment of assessed and due tax from a company in the petroleum sector, where the assessment has become final and conclusive[556] and a demand notice served accordingly on the company, the FIRS to distrain the company by its goods or other chattels, bonds or other securities; or upon any land, premises, or place which is owned by the company[557]. The propriety of this mechanism leaves much to be desired, especially at its exercise appears to be without recourse to the courts.

[551] Section 29(4)-(5) FIRS Act 2007.
[552] Section 29(7) FIRS Act 2007.
[553] See Third Schedule to the Act.
[554] Section 29(7)(a)-(e) FIRS Act 2007.
[555] See op cit, Arogundade, pp. 367-371 on the general history of this enforcement aid in Nigerian taxing statute.
[556] See above, n. 514, p. 195.
[557] Section 33(1)(a)-(b) FIRS Act 2007; see also section 86 CITA 2004.

Accordingly, it has been asked, whether the FIRS is to dispense with the litigation of defaulters before the High Court? Or whether the provision is intended to be an enforcement tool to be used only as a last resort, after litigation has been concluded in the courts?[558]

The answer, it is submitted, is that the tool is one of last resort. That is, before the warrant of distraint[559] can be issued by the executive chairman of the FIRS, it has a duty to exhaust the legal remedies of civil action in the court. This is because the law states that without prejudice to any other provision of the Act or any other taxing statute any amount of tax due constitutes a debt due to the service and recoverable by a civil action brought by the FIRS[560]. This apparent inconsistency between the two provisions of the same law, must be, regard being had to the principle of interpretation of statutes, resolved in favour of the latter, that is section 34. The civil action ripens where the taxpayer has defaulted but only in respect of an assessment that is final and conclusive.

Thus, it is submitted that the process of exercising the power of distraint will be as follows: one, where the Tax Appeal Tribunal (TAT) gives a decision, and the tax is not paid within the one-month period, the proper course to take is for the FIRS to proceed to the court to press for recovery in a civil action. Or in the case where the assessment is not contested, the FIRS will still proceed to the court to press for recovery; two, where the court gives judgement for the FIRS, the taxpayer has six months to pay the judgement debt plus interest. Where the debt remains unpaid, the executive chairman can now issue warrant of distraint. However, it is submitted that, on the basis of *ex*

[558] Op cit, Arogundade, p. 369.
[559] See Fourth Schedule to the FIRS Act 2007; Fourth Schedule to the CITA 2004.
[560] Section 34 FIRS Act 2007; section 87 CITA 2004.

abundante cautela, the best practice should be for the executive chairman to seek, *ex parte*, an order of the court to enforce its judgement through the mechanism of distraint. That way, the exercise of this power will be fair, just and equitable both to the FIRS and the defaulting taxpayer.

Notwithstanding the above provision, it has been decried that the power has neither been tested in court nor put in practice[561], there being no record of the exercise of the power[562] of distraint either by the FIRS or its predecessor FBIR. Thus, the present practice is for the FIRS to retain due but unpaid taxes on the **Arrears List** as bad and irrecoverable debts to be presented to, and approved for write-off by, the Public Accounts Committee[563]. This practice has the potential of depleting accruable revenue to the government, especially in these days of dwindling fortunes for the oil, exacerbated by the rising profile of alternative sources of energy to the oil. By engaging in this practice, it renders nullity the essence of the provisions. The provision is meant to enable the FIRS to recover tax debts from the sale of the property, whether movable or immovable[564], of the judgement debtor.

However, it must be pointed out that failure to pay tax debt might not be intentional, as some of the "tax debtor companies were owed staggering amounts by the agencies of government for jobs executed but not paid for by the government and in respect of which assessments had been raised"[565] by the FIRS, an agency of the same government. Thus, non-enforcement or

[561] Op cit, Arogundade, pp. 369-370.
[562] Op cit, Arogundade, p. 371.
[563] Ibid, Arogundade, p. 370.
[564] See section 33(6) FIRS Act 2007, which limits the power to sell immovable subject to the order of a High Court.
[565] Op cit, Arogundade, p. 371.

apparent unwillingness to engage this power by the FIRS might border on moral grounds, which is understandably good wisdom.

5.4.4 *Whistle Blower Provision*. For the first time, the FIRS is encouraged to enlist to cooperation of the public in order to enhance the performance of its duties, which is principally the enforcement of the provisions of the CITA and PPTA, amongst other taxing statutes. Thus, subject to the approval of the FIRS Management Board, the FIRS have power to pay any reward to any person who volunteers information that may be of assistance to the FIRS in the performance of its duties. The payment of reward is subject to meeting the conditions determined by the Board, and the quantum of such reward shall also be at the discretion of the Board. Importantly, the identity of the person must be kept confidential.[566]

Laudable as the above provision may appear, it is submitted that it is neither here nor there as to be capable of eliciting the needed public patronage. First, the FIRS is not at liberty to take the decision to reward, but it must seek the approval of the Board, and the latter has the power to determine the amount of reward and the conditions for giving the reward. This is an unnecessary red tapism, which will only exist to ensure that the provision is never implemented. Second, the FIRS is far removed from the public, that it is seen as an enemy rather than a friend. It is expected that the element of 'service' which its supposed name is meant to espouse will come alive. In other words, the FIRS must be service-oriented, before it can commend itself to the confidence of the public. Otherwise, the whistle-blower provision will remain

[566] Section 37(1) and (2) FIRS Act 2007.

relevant only in the imagination of the FIRS. This means that as presently constituted the end of the provision will hardly be served.

5.4.5 *Powers of Investigation*.[567] This is also a novel provision in our fiscal laws. One it empowers the FIRS to engage the services of Special Purpose Tax Officers (SPTO), who are specially designated tax officers primarily involved in tax investigation and tax enforcement. They have the powers of police officers[568]; hence they can make arrests, with or without warrant, of any person who committed, or is committing, or is suspected of having committed, or is about to commit (attempt) a tax offence.[569] In furtherance of this investigatory power the FIRS can investigate or cause investigation to be conducted into the affairs of any petroleum operations company to ascertain any violation of the fiscal laws relating to petroleum operations in Nigeria, whether or not it received a report of any violation.[570] This means that there is no hurdle standing in the way of the FIRS from investigating any case of suspected violation of fiscal laws relating to the petroleum sector of the Nigerian economy by any company. It equally means that the FIRS is now positioned to enforce the observance of the fiscal laws more than ever before.

While going about its duties of investigation, the FIRS through the SPTO can cause investigation to be conducted into the properties of any taxable person if it appears to the FIRS that the lifestyle of the person and extent of the properties of the person are not justified by his source of income[571]. This provision, it is submitted, is targeted at executives of petroleum operations

[567] Section 35(1) FIRS Act 2007.
[568] Section 69 FIRS Act 2007.
[569] For example see sections 10 Criminal Procedure Act; section 26 Criminal Procedure Code; and section 24 Police Act.
[570] Section 35(2) FIRS Act 2007.
[571] Section 35(3) FIRS Act 2007.

companies, who may be milking their companies, while the government is denied of its due share in taxes, fines, dues and royalties. This is not surprising for the executives constitute the brain and the mind of the company. This mind could be exercised to further the self interests of the executives, and where this is the case, as is usually so, consequential tax offences are bound to be committed, for instance, tax evasion.

The problem with this provision is that of enforcement. The SPTOs must be specially trained personnel, not just specially designated personnel. This is because if you specially designate a person as someone while he is not fit, in terms of skill, competence and experience, to be that someone, you are creating more troubles for the person and for the system. Unless conscious efforts are made at training and equipping the SPTOs technically, nothing can be achieved of this provision. Also, the angst is that the SPTOs, either acting alone or in concert with government of the day, could use the provision as a willingly ready weapon of oppression, witch-hunting and score-settling.

5.4.6 *The Role of the Tax Appeal Tribunal (TAT).* Where the FIRS is aggrieved by the non-compliance by a downstream or an upstream company in respect of any provision of the relevant fiscal laws relating to petroleum operations in Nigeria, it may appeal to the TAT by giving notice in writing to the secretary[572]. Where it relates to self assessment, to call for further returns, or request for information by banks, etc, the proper forum is the TAT. However, where it relates to collection of tax on assessments that are final and conclusive, it is submitted that the court is the proper forum, having regard the need to exercise distraint powers.

[572] Section 59 and para 14, Fifth Schedule to the FIRS Act 2007.

CHAPTER SIX

SUMMARY, CONCLUSION AND RECOMMENDATIONS

6.0 SUMMARY

The fiscal policy effectually strikes a balance between the resources the government puts into the economy through expenditures and that it takes out through taxation, charges, or borrowing. When government takes the bold step of concretising its fiscal policy the end product is laws, for instance tax laws. Thus taxation is an inherent element of fiscal policy. The petroleum industry as a major revenue earner for the government is not immune from this inherent element. However, concerns surround the efficacy of the fiscal law relating to petroleum operations having regard to the hackneyed calls for, and untiring efforts at discovering, cheaper alternative sources of energy, in a world whose economic activities are now unleashing backlash effects in the form of ozone layer depletion, global warming and other environmental concerns.

Chapter two looked into the Nigerian petroleum generally. The history of the Nigerian petroleum industry is traceable to 1908, when a German entity, the Nigerian Bitumen Corporation, began, unsuccessfully, exploration activities in the Araromi Area, West of Nigeria, albeit these pioneering efforts were abruptly disrupted by the outbreak of the World War I in 1914, However, full exploration activities began in 1937 Shell D'Arcy was given the whole concessionary rights to explore for oil. It was not until 1957 that the first commercial discovery was made in Oloibiri in the present day Bayelsa State.

Petroleum is a multifaceted product. Basically, the Nigerian petroleum industry is divided into two broad categories: upstream operations and downstream operations. There is an adjunct to the petroleum industry, natural gas operations. Upstream

operations involve exploration and production of crude oil, under governmental grant of licence[573] by companies for sale or disposal. On the other hand, downstream operations involve those activities which culminate in value addition and improvement upon the end product of upstream operations. As disclosed in the research, different fiscal regimes govern the two categories. For instance, the Petroleum Profits Tax Act amongst other fiscal enactments relate and govern upstream operations; while Companies Income Tax Act and other related fiscal laws relate and govern operations in the downstream sector. Generally, the recently enacted Federal Inland Revenue Service Act 2007 relates and governs operations and activities in both categories.

Generally, the structure of Nigerian petroleum operations discourages participation of Nigerians, and this could have implications for revenue base of the country. This explains the Nigerian content initiative of the government. The Nigerian Content is defined as the quantum of composite value added or created in the Nigerian economy by a systematic development of capacity and capabilities through the deliberate utilization of Nigerian human, material resources and services in the Nigerian oil and gas industry. The above statutory definition is not good enough as it failed to recognise the need to make it a condition precedent that for utilization of such Nigerian element must be within acceptable quality, health, safety and environment standards, so that Nigerian content should not be taken as a safe harbour to harbour mediocrity in this sensitive sector. It has also been stated that the objective of the local content development is to significantly increase the contribution of the expenditures in the upstream sector to the Gross Domestic Product (GDP) over a defined period of time. Therefore, the Nigerian Government seeks to stimulate and

[573] Under the Petroleum Act CAP. 350 L.F.N. 1990; ACT CAP. P10 L.F.N. 2004, there are three types of licences granted by the government, namely ***oil prospecting licence, oil mining licence and oil exploration licence.***

develop local capacity in the Nigerian oil and gas industry. By so doing, Nigerians would be empowered to participate actively and massively in the oil and gas industry, particularly in the upstream sector. This affirmative action has become a law with the passage of **Nigerian Oil and Gas Industry Content Development Act 2010**.

Since its discovery, in preindustrial time to the era of industrial revolution and up to the present day, petroleum has become a pervasively multifaceted product that affects the lives of all humanity in one way or the other, and at every level. Petroleum is first among other energy sources. Hence, modern industrial civilization depends on petroleum and its products; the physical structure and way of life of the suburban communities that surround the great cities are the result of an ample and inexpensive supply of petroleum. Petroleum and its derivatives are used in the manufacture of medicines and fertilizers, foodstuffs, plastics, building materials, paints, and cloth and to generate electricity. In fact, the goals of developing countries—to exploit their natural resources and to supply foodstuffs for the burgeoning populations—are based on the assumption of petroleum availability.

Historically, petroleum operations in Nigeria is said to have evolved in phases – the first phase covering the periods of 1900 to 1959; and the second phase covering the period 1960 to date. The first phase was marked by the upsurge in oil exploration activities traceable to 1908, "when a German entity, the Nigerian Bitumen Corporation" began, unsuccessfully, exploration activities in the Araromi Area, West of Nigeria, albeit these pioneering efforts were abruptly disrupted by the outbreak of the World War I in 1914. It was not until 1951 that Shell-BP successfully drilled its first well "at a location near Ihuo village, some sixteen kilometres north-east of Owerri. Finally, the efforts of Shell-BP paid off when in 1956 it made its first

commercial discovery in a location near Oloibiri in present day Bayelsa State, with a production capacity of 5,100 barrels per day in 1958.

The commercial find consequently led to the enactment Oil Pipelines Act of 1956 (CAP 145 of the 1948 Edition of the Laws of Nigeria; Petroleum Profits Tax Act 1959 (made to have a retroactive effect), etc. Then, the second phase which starts from 1960 to date. During this phase Nigeria is now entrenched as oil producing nation, with massive reserves. This era undoubtedly witnessed, and is still witnessing, the highest number of activities as it is within this era that oil took the centre stage as the main stay of the Nigerian economy. In the early stages of this, precisely 1970s, Nigeria, prompted by many factors, began to create institutional framework for direct government participation in petroleum activities. This led to the creation of the Nigerian National Petroleum Corporation (NNPC), the successor to the Nigerian National Oil Corporation (NNOC). Thus, the NNPC was charged with responsibility over the exploitation and exploration activities including end-point stage activities (for instance, refining, marketing and distribution).

Petroleum operations means all activities of prospecting, exploration, exploitation and transportation of hydrocarbons, comprising the storage and processing thereof, especially, the natural gas processing but it does not comprise the refining and distribution of petroleum products. However, in this Research and despite the clear but restrictive statutory meanings given to the term, petroleum operations shall widely be construed to include the downstream operations (that is refining and distribution of refined petroleum products). Thus the fiscal laws relating thereto (i.e., downstream operations) shall, with equal force, be considered.

In Nigeria, various legislations impinge upon petroleum operations and they include in the main Petroleum Act CAP 350 LFN 1990; CAP P10 LFN 2004 (with its subsidiary legislation that is the Petroleum (Drilling and Production) Regulations 1969; Petroleum Products Pricing Regulatory Agency (Establishment) Act No. 8 2003 (with its 2004 amendment); Companies Income Tax Act CAP 60 LFN 1990; CAP C21 LFN 2004; Companies Income Tax (Amendment) Act 2007; Petroleum Profits Tax Act CAP 354 LFN 1990; CAP P13 LFN 2004; Deep Offshore and Inland Basin Production Sharing Contracts Decree No. 9 1999 (now CAP D3 LFN 2004). There is also Deep Offshore and Inland Basin Production Sharing Contracts (Amendment) Decree No. 26 1999; Nigeria LNG (Fiscal Incentives, Guarantees and Assurances) Decree No. 39 1990 (now CAP N87 LFN 2004). The principal Decree was amended by Nigeria LNG (Fiscal Incentives Guarantees and Assurances) (Amendment) Decree 113 1993; and Federal Inland Revenue Service (Establishment) Act 2007.

Despite the cries of dwindling revenue from petroleum and its derivatives, it has been projected that world oil demand is expected to rise through the year 2010 (and beyond) at a rate of about 2 percent per year for oil and 3 percent per year for gas, (essentially because of) the significant benefits of hydrocarbon energy – namely, its low cost, its ease of use and its flexibility to enhance our lives in multiple applications. But the "catch is that while demand increases, existing production declines". This means that the fears over the new U.S. energy policy and the quest for renewable energy need not be a concern at least in the immediate, because there will always be willing buyers for our goods, oil and gas. However, Nigeria may not be able to meet the surging world demand for oil and gas, leading to a depletion of revenue. This is because the nation's production capacity continues to fall because of the renewed and

fierce militancy in the region. The August 2009 Amnesty Deal however appear to be yielding results as restiveness and militancy have significantly ebbed away.

Obviously aware of the need to reposition the petroleum industry, the government embarked on a reform agenda. This agenda is propped by the Petroleum Industry Bill 2008. The Bill is said to be the most far-reaching and most comprehensive piece of legislation with over 500 provisions and covers virtually every aspect of governance and operations across the petroleum industry value chain, ranging from fundamental objectives of state policy, institutional framework, upstream and downstream operations, fiscal system and to matters of health, safety and environmental and community relations. The bill will among other things unbundle the NNPC into autonomous units. The Bill has been criticised as a potential dysfunction to investment in the sector, essentially because many provisions in the bill are unclear and open to multiple interpretations which would substantially increase investment risk, comparatively placing Nigeria at a disadvantage for inflow of foreign investment. It would appear that the Bill has died naturally since nothing has been heard of it since the passage of the Nigerian Oil and Gas Industry Content Development Act, perhaps as a compromise position between the government and the International Oil Companies, the major opponents of the Bill. If this is so, it is sadly regrettable.

There are various types of legal arrangements for upstream petroleum operations in Nigeria which have implications on the revenue accruable to the government. These are “the concession”, “the joint venture, represented by the Joint Operating Agreement (JOA)”, “the production sharing contract (PSC)”, “the service contract”, and arrangements involving indigenous companies and marginal fields, known as sole-risk. But under the PIB, **Article 272(2**) specifically provided for three model

contracts which the National Oil Company or any other oil company is empowered to enter, namely Production Sharing Contracts; Risk Service Contracts, which provides for reimbursement of the oil company contractor for costs where a discovery is made and shall be entitled to payment in cash or from crude oil or natural gas produced from the contract areas; and any contract being a variation of production sharing contracts or risk service contracts, which for the time being is an internationally acceptable mode of awarding contracts for exploration and production of oil or natural gas, as the case may be.

Chapter Three focussed on the fiscal laws relating to upstream operations of the Nigerian petroleum industry. These are the PPTA, the PSC Act, and the Incentives Act. Subject to its passage into law, the aforementioned laws, save the Incentives Act and section 16 subsections (1) and (2) of the PSC Act, will be repealed by the Nigerian Hydrocarbon Tax under the Petroleum Industry Bill 2008 currently before the National Assembly for enactment into law. Under the PPTA, private individuals or partnerships are precluded from engaging in petroleum operations, apparently due to the huge capital outlay involved. On the flip side, no tax shall be charged under the provisions of the Personal Income Tax Act or any other Act in respect of any income or dividends paid out of any profits which are taken into account, under the provisions of this Act, in the calculation of the amount of any chargeable profits upon which tax is charged, assessed and paid under the provisions of the PPTA. This provision is hard to justify since all dividends received by an individual from other corporate undertakings are subject to tax. It is the individual who is being taxed of income from a source inside or outside Nigeria, not the company that paid the petroleum profits tax.

The PPTA is the main fiscal law regulating upstream operations. Yet is possible to find where a company engaged in upstream operations is equally engaged in the transportation of chargeable oil by ocean going oil-tankers. Where this is the case, then such adjustments shall be made in computing an adjusted profit or a loss as shall have the effect of excluding therefrom any profit or loss attributable to such transportation. Thus a company subject to PPTA can under this circumstance be likewise subject to CITA, as if it is a downstream company. This is a balanced position of the law since transportation qua transportation has nothing to do with winning and obtaining oil; charge under PPTA would work injustice since a higher rate of tax will be used; even where the company transports its own oil, it is a deductible expense; and being a different undertaking it cannot be said that the company is subject to double taxation.

On the one hand, the PPTA attempted to tackle tax avoidance schemes of companies, by disallowing interest on intra-company loans or loans between connected companies. On the other, it grants incentives to companies involved in gas utilization projects, both associated and non-associated. Accordingly investments, for instance, required to separate crude oil and gas from the reservoir into usable products shall be considered as part of the oil field development and thus tax deductible. It is submitted that despite this provision, gas utilization projects remain low, for example companies continue to flare out gas. Apparently, this must have informed its removal from the Petroleum Industry Bill 2008.

Further, under the PPTA the chargeable profit is the amount of assessable profit less deductions. Subject always to a threshold of 15% minimum tax, under the PPTA tax is a proportion of assessable profits. This means that if in any accounting period the

tax payable by an upstream company must not be less than the threshold. Where the tax would be less than the minimum threshold, the company must revert to the second formula in which case it will end carrying over allowable deductions to the next accounting period, in so far as the minimum tax of 15% or more is available to be paid for any accounting period. The assessable tax is 65% or 65.75% or 50% for concessionaires under the PSC; under the PIB it is 30% or 50% depending on the geographical zone. The innovation in the PIB is that all upstream companies shall now be subject to CITA in addition to PPT payment. This means that the minimum tax under the PIB is 60% and maximum is 80%.

Under the PPTA the chargeable tax is the assessable tax less investment tax credit. however, additional tax may be chargeable especially if in any accounting period of a company the amount of the chargeable tax for that period is less than the posted price, the company shall be liable to pay an additional amount of tax; being the difference between the two amounts. The posted price is periodically revised in order to take advantage of the benefits dictated by favourable market conditions, as such long-standing commitments are not made by the NNPC.

Following the oil glut of 1980s, the government introduced the concept of MOU, which is an agreement between oil companies and the NNPC, representing the Federal Government, representing a package of fiscal incentives to enhance crude oil export, encourage investments in exploration and development activities, encourage investments in enhanced oil recovery projects and encourage investments in gas utilization. The object of the MOU, expected to last for five years, was to minimise the tax liabilities of the petroleum operations company. The MOU was supplemented by Side Letters from the NNPC. The MOU is a disincentive to revenue accruable to the

government. It has fiscal attraction and incentives for an oil company which was why the latter preferred to arrange its affairs in order for its profits to come within the application of the MOU as against the PPTA's strict provisions are still very much present. In an case the conditions which led to the MOU are no longer obtainable, especially with current rising oil prices.

Under the PSC regime, the contractor finances the operations while the concession holder shares in the profit. The applicable tax rate is a flat rate of 50% of chargeable profits; while an ITC of 50% of qualifying expenditure for contracts executed before 1/7/1998 and investment tax allowance (ITA) for subsequent contracts are applicable. Oil-blocks are ring-fenced so that a loss from one oil block cannot be set off against profits from another oil block. Payment of tax is in kind, by the allocation of tax oil to the NNPC for payment of PPT on behalf of both parties. The PSC is apparently attractive to the government since the burden of meeting cash call obligations which marred the JVC operations is eliminated. However, it is undoubtedly attractive to the contractors as tax liability is much reduced. However, the concession holder bears the risk of loss arising from each block, since loss cannot be set off against the profits from another block.

Tax payments under the PSC and PPTA appear confused due to the issue of ITC and ITA. This is because under the PPTA, the issue of ITC and its application amounts to absurdity as it leaves the contractor without any tax liability or obligation. However, this cannot be taken to be the law, especially as the PSC Act voids any provision of any other law or enactment which is inconsistent with its provisions. Thus, the provisions of the PPTA on ITC and its absurd consequences have been taken care by the PSC Act. On the other hand, the PSC has been criticised. For example, the allocation of cost oil

to the contractor in such a quantum as to generate an amount of proceeds sufficient to cover operating costs is shrouded in secret dealings between the NNPC and the contractor. This means the process is anything but transparent.

The Incentives Act is the real legislative faux pas. It grants 10 year tax holiday to the NLNG, while the needs for revenue increases at astronomical levels. It excludes the participation of Nigerians in the natural gas operations. It has outlived its usefulness. Other fiscal matters which relate to petroleum operations and which are sources of revenue to the government include bonuses, fees, royalties, oil terminal dues, etc. Fees are payable in respect of an OPL and OML and they constitute fiscal outlay to the government; bonuses are premiums payable which represent monetary consideration for grants of OPL, PSCs and marginal field allocations; and royalty is payable by the producer on the quantity of the oil produced at the percentage fixed by law and can by paid wholly or in part, in kind to the government.

Chapter Four is concerned with the fiscal laws relating to downstream operations in the Nigerian petroleum sector. The principal enactment here is the CITA. The core activities involved in downstream operations, which fell within the CITA consist of transportation of crude oil by ocean going tankers from Nigeria to another country; oil refinery; oil distribution and marketing; servicing operations in the upstream sector; and utilisation of associated and non-associated gas.

As regards transportation, the three types of transportation as far as evacuation of crude include where the upstream petroleum operator has his own ship for the transportation of the crude to his refinery or to the spot market (that is it is a separate and distinct business of the upstream operator); where the operator, like the NNPC, has no ships of his own but allows buyers of the crude to bring their own ships

for the evacuation of the crude (in which case section 14 CITA); and where the buyer or the operator has no ship of his own but hires ships for the transportation of the crude (where the hirer is paid is rent, making the CITA applicable).

As to other activities involved in downstream operations these will include oil refining and oil servicing activities for example. Oil refining is a manufacturing activity, and the profit therefrom is assessable to tax under the relevant charging section of the CITA; while oil servicing activities include surveys, drilling, catering, hire services, finance, supp of equipment, property and know-how and other forms of technical, consulting or management services. Under CITA oil servicing, activities, though carried on by the same company, may be differently characterised for tax purposes, meaning that under the CITA different rates may apply.

The business of petroleum marketing companies involves trading in refined petroleum products; there are servicing companies whose business involves procurement, maintenance of facilities and infrastructure deployed to rigs by upstream petroleum operations companies; and yet there are others whose business border on services which may be technical, consultancy, agency, management or contract. All these activities, normally contained copiously in the objects clause of such companies, whether trading activity or services activity, are subject to corporate tax. The tax treatment of trade receipts and service receipts are not the same. While service receipts (fees) are subject to source deductions, business receipts are not subject to withholding since they do not come under the source deduction rules under section 94 of CITA 2004.

The business receipts of a company may be revenue in nature or capital receipts. The former is assessable to tax as a source of income, while the latter is not. Thus, revenue

receipts assessable to tax are receipts that recur as against those that are once and for all receipts which are capital; a lump sum payment which amounted to surrender of the congeries of rights under a joint operating agreement, being a capital receipt, is not assessable to corporate tax; and any payment received for the termination of a contract agreement which effectually affected the whole profit-making outfit of the taxpayer, such a termination agreement not being an ordinary commercial contract made in the ordinary course of business, is a capital receipt. The distinction between capital receipts and revenue receipts is important because capital receipts are taxed under a separate taxing statute, the Capital Gains Tax Act; while revenue receipts are properly taxable under the CITA.

Further, there are certain situations in which the profits of a downstream company may be exempted from payment of corporate tax. Thus, where any Nigerian company operating in the downstream industry is engaged wholly in export oriented business, its profits shall be exempt from corporate tax in respect of goods exported from Nigeria, provided that the proceeds from such export are repatriated to Nigeria and are used exclusively for the purchase of raw materials, plant, equipment and spare parts; or dividends from investments in wholly-oriented export business. Also, the profits of any downstream petroleum company established within an export processing zone or free trade zone, for instance the export processing zone in Calabar, shall be exempted from corporate tax. Generally, the grounds exempting tax payment are meant to encourage the development of the country's industrial base and generate employment, leading generally to the development and sustenance of a robust economy. However, the same cannot be said of the provision allowing the president to exempt on any ground which appears to him/her to be sufficient. This

provision can be unduly exploited by any person occupying the office of the president who is not guided by the principles of integrity, fairness and equity.

Unlike the PPTA, the basis of assessment of downstream companies is preceding year basis. This basis of assessment is flawed because it is like the government giving taxpayers an interest-free loan, so that in times of inflation the government would not only lose the interest but also the value of the currency would have declined. It is equally flawed because the lag in the payment under the preceding year basis tend to create inequities between taxpayers, wage earners and others subjected to withholding tax that are under compulsion of law to pay their taxes on a timely basis. Thus taxation of downstream companies in Nigeria is on their paper profits rather than real income. This position makes the current year system obtainable under the PPTA more preferable.

In ascertaining the tax liability of downstream companies, the correct principles of prevailing system of commercial accountancy are dispensed with. This is because different downstream companies adopt different valuation policies, so that this could result in different profitability positions. Secondly, companies are not to be trusted as they are wont to play around with figures. In order to create level playing field, the law provides for allowable and disallowable expenses, which is applicable to all downstream companies. Yet, it is observed, the field may not be level as some companies are wont to prepare two payslips for their employees, for example. An expense is allowable and deductible if it was wholly, exclusively, necessarily and reasonably incurred for or in the production of the profits of the downstream company. The nature of the business of the company, the circumstances attending to the item of expenditure, the specific environment of the business and other laws

regulating the particular business contribute to influence a decision as to whether an item of expenditure is allowable and deductible and vice versa.

Further for the purpose of ascertaining the profits or loss of any company of any period from any source chargeable with tax, there shall be deducted such other deduction as may be prescribed by the Minister by any rule. The exercise of this direction by the minister must be in synchrony with the omnibus ground, that is such deduction must be wholly, exclusively, necessarily and reasonably incurred in the production of those profits. Also, the exercise of the discretion by the minister must accord with good law, good reason and must be in good faith.

On the other hand, the donation must be made out of the profits of the downstream company are tax deductible. However such donation is limited to ten percent of the total profits of the company; it must be an expenditure of a revenue nature; the beneficiary must fall under the body recognised in the Fifth Schedule of the Act and notwithstanding the latter, the beneficiary must be a public fund, established in Nigeria and having a public character. However the CITA 2007 amendment law has changed the complexion of this item. Thus, a donation to a university, research institution or tertiary institution, whether private or public, is tax deductible. It means that donations by downstream companies to a private cause must be limited to a private educational institution, i.e., a private university or tertiary institution.

Further, it is not every item of expenses in the audited accounts of a downstream company that will be reckoned with in the computation of the company's tax liability in any given financial year. An expense that was not wholly, exclusively, necessarily and reasonably incurred in the production of those profits would be disallowed. Likewise, an expense that has been specifically and expressly disallowed by the taxing

statute will be disallowed, in spite of the fact that it was wholly, exclusively, necessarily and reasonably incurred. Thus, capital repaid or withdrawn and any expenditure of a capital nature, depreciation of any asset, any sum recoverable under an insurance or contract of indemnity, penalty for unlawful act since this cannot be said to have been necessarily incurred, any general reserve, general provision or contingent liability or an expense that cannot be ascertained with substantial accuracy, etc are not allowed in ascertaining the profits of any company.

In addition, in computing the total profits of a downstream company during any preceding year of assessment, the law ordains that any losses incurred by the company shall be deductible. However, the aggregate deduction from the profits must not exceed the amount of the loss – that is, the downstream company is obligated to deduct 'actual', and not manipulated 'book', losses. Two, the amount deductible is limited to the amount of assessable profit included in the total profits for that year and derived from the source in respect of which the loss was sustained. Loss deduction is income source dependent. Three, the loss can be carried forward and set off against the profits from the same income source subject to a maximum period of four years and any unabsorbed losses lapses thereafter.

Moreover, in computing the tax liability of a downstream company various capital allowances are tax deductible. They are initial allowance, annual allowance, investment allowance and balancing allowance. It is wise tax planning strategy to claim investment allowance ahead of initial and annual allowances. This is because investment allowance is not reckoned with when determining the tax written down value of the asset, and it cannot be carried out where it is not utilized in the year in which it is claimed. On the other hand, balancing allowance arises where the asset is

disposed of and the proceeds of the disposal are lower than the residual value of the asset. It is the difference between the residual value and the sale value.

Conversely, there is a provision as to balancing charge, which is a reverse to balancing allowance. It obtains where the value of an asset at disposal is higher than its residual or written-down value, the excess will be reckoned as profit. The asset must be in use immediately prior to its disposal and the charge must not be higher than the total allowances already granted. It is hardly that companies operating in the downstream petroleum sector will disclose such cases where the disposal of an asset exceeds its book value. Thus the only case where the FIRS will bring this provision to bear on the practical plane is where a transaction is artificial or between the company and a fictitious person or an entity. In such a case, if the FIRS will form an opinion that the open market value of the asset is far in excess of the disposal value and the residual value, then the issue of balancing charge will arise.

In order to encourage industrial renewal and sustenance of productive capacity, the law provides for allowance of 15 percent ITC, which is a set off against the tax payable, unlike investment allowance which is deductible from the assessable profit of downstream company. There is another incentive to companies engaged in downstream gas utilization operations. Thus, the law provides that they shall be granted an initial tax-free period of three years which may, subject to the satisfactory performance of the business, be renewed for an additional period of two years. This means that the company is subrogated in the position of a pioneer company status that equally tax holidays of up to a maximum of five years. However the affected company must choose between appropriating the provision as to tax free period up to

a maximum period of five years and claiming an additional investment allowance of 35 per cent.

Despite the mouth-watering incentives granted to downstream companies engaged in gas utilization operations specifically, and the downstream companies generally under the taxing statute, it is equivocal that tax incentives are not the answer to Nigeria's quest for investment. Rather, the factors that act as disincentives need to be addressed. These factors are security, convertibility of local currency, political stability, markets, the legal-regulatory environment and corporate governance.

In Chapter Five the administration and enforcement of the fiscal laws affecting petroleum operations in Nigeria were considered. Principally, this brought to focus the role of the FIRS and the establishing Act, which was recently enacted in 2007. Generally, the FIRS was established in order to give 'teeth' to the enforcement of the fiscal laws relating to petroleum operations in Nigeria. Consequently, Part I of the CITA was repealed. Inadvertently, Part II of the PPTA was left intact. As to the latter, there is no cause for alarm, and no purpose is served dancing around technicalities, when regard is had to rule of interpretation.

Principally The FIRS was established to control and administer the different taxes and laws specified in the First Schedule to the FIRS Act or other laws made or to be made, from time to time by the National Assembly and to account for all taxes collected. Accordingly, the FIRS is seized with some statutory functions, which, amongst others, include to assess companies chargeable with tax; to assess, collect and account and enforce payment of taxes as may be due; and to adopt measures to identify, trace, freeze, confiscate or seize proceeds derived from tax fraud or evasion.

It is a legal fact that minister of finance has general supervisory powers over the FIRS and may give directives of a general nature or generally relating to matters of policy with regards to the exercise of its functions, including in the administration of the CIT or the PPTA. However, no company should be advantaged or disadvantaged on account of any direction or order or instructions from the minister. In other words, any direction, order or instruction, which confers undue advantage or imposes undue burden on a company, will be ultra vires the minister and the FIRS is not bound to obey. This is because it will amount to illegality if duly executed by the FIRS.

One of the core functions of the FIRS is assessment. Thus, two types of assessment are obtainable: self assessment or FIRS assessment (government assessment). Companies in the downstream companies are now bound to compulsorily make and file assessment. This means that anytime the FIRS makes assessment on a downstream company, it is will be doing so with a penalty for late filing against the company. However, under the PPTA the duty to make assessment lies with the FIRS, which assessment shall derive from the accounts and particulars together with returns filed with the FIRS not later than two months after the commencement of each accounting period. The system of government assessment under the PPTA survived in the Petroleum Industry Bill 2008. The assessment function of FIRS also arises where a company fails to deliver a return – in which case the FIRS has power to use best of judgement to determine the amount of the total profits of the company and make assessment accordingly. Equally, the FIRS has power to make additional assessment upon any company, consequent upon the discovery of new facts. This means that it is immaterial if it will mean reopening an assessment that has become final and conclusive. It must be noted that additional assessment is time-bound, so that any

additional assessment made out of time, will be statute barred. Moreover, the taxpayer has right of objection against any assessment made on it by the FIRS.

As regards collection, the function of the FIRS is made easy in respect of downstream companies that are expected to make self assessment, and show proof of payment of part or whole of the self assessed tax. Where it is FIRS assessment, the taxpayer is expected to pay within two months. However, the FIRS assessment is subject to technicalities. For instance, it is not final and conclusive, since the right to objection, within the time specified for making such objection, avails to the taxpayer. Yet, a company cannot, under the disguise of objection to an assessment, be allowed to fish for skirmishes. For example, an assessment shall not be impeached or affected by reason of a mistake as to the name of the company liable to tax.

To enhance the administrative function of the FIRS, certain powers in aid of enforcement were donated to it under its establishing Act. One, the FIRS has the power to call upon any bank to deliver to it information relating to any company in the petroleum sector, whether downstream or upstream. This provision enables the FIRS to track the activities of companies so that the veracity of the returns filed by the companies, pursuant to self-assessment, can be subjected to objective scrutiny. However, failure to oblige the information attracts a fine of N500,000, which penalty cannot be said to be potentially deterrent. Two, the FIRS has right of free access to all lands, buildings, places books and documents, whether stored in electronic media or any other form, in the custody or under the control of a public officer, institution or any other person, for the purpose of collecting any tax.

Third, the FIRS have distraint powers, one which is said to be a tool of last resort. It means that the power becomes exercisable where the court has given judgement in

favour of the FIRS and the judgement debt remains unpaid after the requisite period. On the basis of *ex abundante cautela,* the FIRS, *ex parte*, will approach the court for an order to distrain the defaulting taxpayer (whether downstream or upstream operator) by its goods or other chattels, bonds or other securities; or upon any land, premises, or place owned by the taxpayer. The power of distraint has been in the books only as the current practice is for the FIRS to retain due but unpaid taxes on the **Arrears List** as bad and irrecoverable debts to be presented to, and approved for write-off by, the Public Accounts Committee. This practice renders nullity the essence of the provision relating to distrainment, which is to enable the FIRS to recover tax debts from the sale of the property, whether movable or immovable, of the judgement debtor.

6.1 CONCLUSION

From the issues which this research has addressed, it is apt to infer the following:

A. Despite the hues and cries over dwindling oil demand, and its consequent effect upon the revenue base of the government, the cry is far from the reality on ground. Oil and gas are expected to remain the leading energy sources for some time to come, meaning that their demand will continue to increase. Secondly, the supply of oil and gas is essential to sustaining economic growth in the industrialized world and it is fundamental to progress in nations (e.g., Nigeria) working their way towards prosperity. There is general distrust of renewable energy as a low energy diet, notoriously unreliable and inefficient. With these insights, the likely advent of cheaper sources of alternative energy will remotely impact upon the revenue base of the country, since petroleum still holds the key to economic growth.

B. Despite the promising future of oil and gas as the number one preferred source of energy, the Nigerian case is a peculiar one. While the other world producers of

oil and gas battle with depleting supply of this energy source, Nigeria's case would be compounded by militancy and restiveness in the oil-rich Niger Delta region of the country. This means that even if the supply of oil and gas is readily and assured and the fiscal laws regulating the petroleum operations in Nigeria are effectively efficacious, Nigeria will still have to grapple with the regrettable activities of militants. However, with the announcement and implementation of amnesty programme by the Government in August 2009 all appear to be well in the region. Thus, with government commitment and sincerity towards the amnesty initiative, the danger that militant activities posed to the supply of oil and gas in and by Nigeria will be a thing of the past. In the final analysis, this leaves the question of the role or efficacy of the fiscal laws relating to petroleum operations as one of the principal determinants of the extent of accruable revenue to the government from petroleum operations.

C. The fiscal laws relating to upstream operations appear to be on a collision course, with a tendency that the capacity of the government to generate revenue will be much reduced. The seeming inconsistencies between profit sharing contract under the PPTA and profit sharing contract arrangement under the PSC Act is a case in point. For example, under the PPTA ITC being 50% of chargeable profit is deductible from assessable tax, with the effect that nil tax is achieved; while under the PSC Act ITC is 50% of qualifying capital expenditure. Except the FIRS insists on curing the manifest absurdity, of course assuming that their independence is fettered by underhand dealings, the operators are wont to exploit this gaping hole and inconsistency in the law.

D. The NLNG has become a conduit pipe for depriving the nation of scarce resources, especially in this sobering period of economic meltdown. The

avalanche of incentives and assurances granted to it is simply arm twisting, which the government ought to have wriggled itself out from. To state that the company, which is apparently an upstream operator, shall not be liable to the PPTA, since it is not a law that is generally applicable to all companies in Nigeria, is regrettable, and an undoubted case of economic emasculation of the Nigerian people. Sadly, the anomaly appears to go unnoticed since the Incentives Act was not one of the enactments slated for repeal under the almost dead and forgotten PIB 2008. While the generality of Nigerians suffocate from the asphyxiating effects of the law through the denial of revenue badly needed for infrastructural development, it might be that a few are having a field day. For example, for the NNPC to claim that it did not have records of natural gas produced or sold by the Nigerian Liquefied Natural Gas (NLNG), after nearly 10 years of its operation, is simply callous and a conscious act to defraud Nigerians.

E. The fiscal laws impacting on downstream operations appear to be quite in order, and capable of ensuring sustained revenue to the government in the face of plummeting oil prices. It must be observed that recently the price of the oil in the international markets has been very encouraging. With the CITA Amendment 2007, downstream companies are expected to show greater compliance, since failure to make a return, with evidence of payment of the whole or part of the self assessment attracts a biting penalty of N25,000 for the first month (i.e., June) and N5,000 for each month that the default continues. Fundamentally, the removal of the one percent bonus for payments by companies that made self assessment and kept to the payment

arrangement will ensure that more revenue will trickle into the purse of the government for financing infrastructural developments and programmes.

F. The presidential power to exempt any company or class of companies from all or any of the provisions of the CITA, or from tax all or any profits of any company or class of companies from any source on any ground which appears to him or her sufficient is an act of legislative bazaar. This because the ground on which the power can be exercised is purely subjective. Secondly, the president, except he is one who is actuated by nationalist and patriotic spirit, may use it as occasion to pay back his friends, cronies, sponsors, godfathers and power brokers and business moguls. Under such a case, which is not far from reality, the revenue accruable to the government, by extension to the Nigerian people, from downstream operations becomes measured in pints.

G. Incentives system is part of taxation. No wonder it is provided under every fiscal law, whether relating to upstream operations or downstream operations. For instance, there are incentives to encourage upstream operators to invest in frontier acreages; there are profusely irrational incentives to the NLNG; and there is generous to downstream operators in the area of gas utilization in line with the government's gas master plan. However, tax incentives are not the answer to Nigeria's quest for investment. Rather, the factors that act as disincentives need to be addressed. These factors are security, convertibility of local currency, political stability and markets. This means that incentives provide avenues for the companies to enjoy tax-free profits at the expense of the country. This might have informed the removal of most of these incentives, except that under the Incentives Act, in the PIB 2008.

This is a welcome development. Its benefits can only be felt if the PIB is passed.

H. The FIRS appears to have been clothed with sufficient power and capacity to administer the fiscal laws relating to petroleum operations in the country following the passage of the FIRS Act. It naturally follows that it is expected that the revenue to be generated from this economic sector should be improve tremendously. However, the effectiveness of the law is dependent on the willingness and preparedness of the FIRS to appropriate its statutory powers. For example, the power to distrain has never been exercised. The practice of retaining due but unpaid taxes on the Arrears List as bad and irrecoverable debts, and subject to the approval of the Public Accounts Committee, writing them off is evidence of administrative lethargy on the part of the FIRS. Further, the whistleblower provision cannot deliver on its mandate, meaning that the FIRS must discover ingenious and innovative ways of going about its administrative and enforcement activities, if the best of the fiscal laws relating to petroleum operations in Nigeria are to be assured. Equally, the power to investigate the affairs of any petroleum operations company and of its officers, though yet to be tested being a relatively new provision, can be a willing tool in the hands of the SPTOs and government officials if not monitored.

I. The PIB is a well conceived law, if eventually passed. It has the capacity to greatly improve the revenue of the government, since it provides for payment of petroleum profits tax and companies' income tax by upstream operators. This means that an upstream operator will not only pay hydrocarbon tax, it will be chargeable to normal companies' income tax. However, it would appear that the international oil companies that strongly opposed its passage

and worked assiduously to deal a death knell on it have succeeded. This is because a compromised position might have been reached with the passage of the Nigeria Oil and Gas Content Development Act 2010. Since the passage of this law, nothing has been heard of the PIB 2008.

6.2 RECOMMENDATIONS

In line with the above conclusions, which rest on the problems of the research, the following recommendations are hereby offered as insurance for increasing and sustaining the efficacy of the fiscal laws relating to petroleum operations in Nigeria.

6.2.1 The good of a law is served by its effectiveness in addressing the absurdities and resolving the mischief for which it is enacted. Thus, it is hereby recommended that the FIRS must overhaul its operational machinery with a view to living out its name for which service is called. In other words, the inclusion of the word SERVICE in its name is an indication that its operations and activities must be service-oriented if compliance and cooperation is expected from the people. In any case, observance of the fiscal laws is key to government generated revenue, so there is no middle ground here. To attain to the level for which it commands the respect, cooperation and commitment of the people, who are meant to observe these laws, the FIRS must embark upon on enlightenment campaigns, taxpayer education and sensitization programmes, introduction of information and communications technology to simply tax payments, among others. It must be noted that the FIRS appears to be taking some encouraging steps in this regard, as jingles, advertorials, billboards are seen which harp on the benefits tax payment, the role of the FIRS, etc.

6.2.2 Although, the FIRS Act provides enforcement powers of the FIRS in respect of actual or suspected tax offences, it will be preposterous to suppose or suggest that the

FIRS can now enforce the tax laws entirely on its own. The point to be made is that the FIRS must be unassuming, and it should seek the cooperation of other law enforcement agencies if it must make a success of its enforcement powers. This is notwithstanding the clothing of the SPTO with powers of police officers. Accordingly, the FIRS must liaise and work in conjunction with the police, the EFCC and the office of the attorney general of the federation. For example, economic and financial crimes have been defined to include, among others tax evasion[574], which automatically vests EFCC with jurisdiction to prosecute the offence of tax evasion. Thus, greater degree of success will be achieved where the FIRS works with other relevant agencies in the administration and enforcement of the fiscal laws relating to petroleum operations in Nigeria. This means that complementarity of action will enhance the efficacy of the fiscal laws relating to petroleum operations.

6.2.3 Related to the above point is the question of compliance. One of the ambits of enforcement of tax laws is securing compliance with the tax laws. It is hereby recommended that the FIRS should strengthen its compliance organs with a view to enhancing the efficacy of the fiscal laws. This means that it must prefer field audit to desk audit of petroleum operations companies. This point is more particularly relevant to downstream companies, who are compelled to make self-assessment. The audit is principally to verify any matter relating to the profits of a company or any matter relating to the entries in any books, documents, accounts or returns, including those stored in a computer, digital magnetic, optical or electronic media[575]. The point being made is that the audit should be on scheduled regular intervals. This is because where the companies are conscious of the fact that field audit will be regularly conducted on their activities and affairs, the tendency to doctor returns with a view to

[574] See section 46 EFCC Act 2004.
[575] See section 17 CITA 2007.

avoiding or evading payment of tax will be much reduced. This recommendation becomes more implicated if considered against the backdrop of compulsory self-assessment and the regime of source deductions, both of which increases the propensity of the FIRS to be complacent as regards enforcing the fiscal laws.

6.2.4 It is strongly recommended that the Incentives Act should be repealed without any further delay or politicisation. This recommendation is harped upon grim realities on the ground. The NNPC could not, or so it claimed, account for, or did not keep records of, exports of the NLNG. This is the height of administrative recklessness. The Incentives Act has economically disenfranchised Nigerians, even in the face of Nigerian Oil and Gas Industry Content Development Act 2010. The Incentives Act is now a conduit through which the revenue of the government is drained, since the NLNG cannot pay tax that is obtainable from its sectoral operations, that is the upstream petroleum sector. The need for social infrastructure, industrial capacity and economic empowerment of the Nigerian people is more today, especially in consideration of the United Nations Millennium Development Goals. The MDG goals and its attainment is a function of the availability of resources. The repeal of the Incentives Act will obviously be step in the right direction.

6.2.5 The fiscal regime for petroleum operations companies under the PIB 2008 is preferred. It is therefore recommended that the Nigerian National Assembly should as a matter of urgency complete the legislative processes leading to the passage of the law. As at the time of this research, the PIB 2008 has undergone second reading in the Senate Chambers. However, it is feared that the Bill might have been compromised following the passage of the Nigerian Oil and Gas Industry Content Development Act 2010. This is because since its passage nothing has been said or heard of the PIB 2008. In fact the occasion of the signing of the Bill into the law was

greeted with fanfare and pageantry, as though we have finally got it right. This is not to discountenance the purposes which the Content Act 2010 aims to serve. But the point is that a higher ideal, and higher and nobler and more sustainable objective will be served if the PIB 2008 is eventually passed and signed into law.

6.2.6 The power of the president to waive tax is without any philosophical basis. It is an instrument to make the rich to become richer, since those who are likely to benefit from the presidential powers are the so-called captains of industry and business moguls, who are president's men and women, and who might be factor in the election of the president. Thus, the president is likely to use this power as a payback time to friends and associates of the president. The taxing statutes are founded upon the basis of the offering a level playing field for all taxpayers. This informed the non-recognition of depreciation by the taxing statutes, because it is subject to differing and often conflicting accounting policies of taxpayers. The removal of this power will increase the revenue collectible from tax and thus help the government to raise the needed resources for the development of other sectors, other than the petroleum industry, of the Nigerian economy.

6.2.7 It has been seen that incentives are largely correlated with the efficacy of the fiscal laws that impinge upon petroleum operations in Nigeria. This is because the basics, in terms of infrastructural amenities, political environment and security, are not yet in place. Thus, it is hereby recommended that the government should play down on emphasizing the issue of incentives, and as much as possible avoid using incentives provision as a bet for companies to take initiatives and direct action to areas which the government seeks to promote. Rather, the government should consciously take steps to lay down a stable foundation for industrial growth and economic activity. If good roads are provided, if power supply is steady and stable assured, if security of lives and property are not compromised and if the political will to develop and entrench robust good governance framework is present, government will witness massive developments in both sectors of the Nigerian oil and gas industry – upstream and downstream.

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