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AN EXPERT ANALYSIS OF THE PROBLEMS, SOCIAL EFFICIENT SOLUTIONS, POLICY DIRECTIONS AND PROSPECTS OF STATE ACQUISITION OF OIL MINING LEASES: THE CASE OF NIGERIAN OML 11

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ABSTRACT

It is general knowledge that the countries that are actively engaged in the exploration and production of petroleum and natural gases exert significant sovereignty over their natural resources. In furtherance of ownership control thereof, foreign corporations seeking to invest in crude oil activities are obligated to apply and acquire legitimate licences without which they are not permitted to meddle in crude oil and gas of the host countries. In some countries such as Nigeria, the ligitimate holder of such licenses may assign same to third parties provided that the terms and conditions of the licenses are met. It is against this background that this expert analysis of Oil Mining Lease Number 11 is undertaken. The analysis evaluates the rights of the third party, Rivers State Government which acquired the remainder of the OML 11 license which was assigned to it by Shell Petroleum Development Corporation (SPDC). It presents the possible problems that Rivers State Government may likely encounter – the likelihood of revocation by the Federal Governemnt; conflict of interest arising from the obligation to protect the environment and the possible loss of equity. It concluded that the acquisition of the 45% share is legitimate but that, the concluded deal may be short-lived in the event of punitive revocation by the Federal Government. It recommend among other things that, Rivers State Government should comply with every primary and secondary obligations attached to the OML 11 to avoid the revocation of the acquired titles to the 45% share. It also recommended that Surface Damages and Compensation law should be enacted by the River State House of Assembly to protect

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the host communities against reckless use of the land surface by the oil companies.

Keywords: OML, Petroleum, Assigment of OML, Revocation.

1. INTRODUCTION

The exploration and petroleum of crude oil often require a significant level of access rights involving lands. Consequently, most oil lands are contracted through the execution of renewable leasehold instruments. A leasehold instrument with regards to oil lands, is enforceable contractual relationship between the mineral interest rights owner and the oil company (the operator of OML joint venture hereinafter referred to as the "Operator"). In certain circumstances, the operator may also need to enter into separate lease contract with the surface rights owners. Such arrangement only happens in a situation where the surface rights owners are completely different entities from the mineral rights owners as it is with the OML 11.

In OML 11 such secondary contractual arrangements should be made between the operator and the host communities. The use of Memorandum of Understanding is outdated, unsustainable and unworkable.

In circumstances where the holder of the mineral rights is the Monarch or national government, legislation are enacted to guide the oil leasing process and procedures. In Nigeria, Section 2(1) of the Petroleum Act authorises the Minister of Petroleum to grant three distinct licences namely: (a) An oil exploration licence, to explore for petroleum; (b) An oil prospecting licence, to prospect for petroleum; and (c) An oil mining lease, to search for, win, work, carry away and dispose of petroleum. It must be noted that the third licence is a lease granted on the crude oil for term of years specified. The Minister reserves the discretion to fix the initial lease tenure.

There are several conditions attached to the lease including that, the oil company (leaseholder) must be a company incorporated in Nigeria. This is in tandem with

the provision of Section 54 of the Companies and Allied Matters Act (CAMA) states that:

> Every foreign company which before or after the commencement of this Act was incorporated outside Nigeria, and having the intention of carrying on business in Nigeria, shall take all steps necessary to obtain incorporation as a separate entity in Nigeria for that purpose, but until so incorporated, the foreign company shall not carryon business in Nigeria or exercise any of the powers of a registered company and shall not have a place of business or an address for service of documents or processes in Nigeria for any purpose other than the receipt of notices and other documents, as matters preliminary to incorporation under this Act.

The implication of Section 54 of the CAMA is that the requirement for incorporation as Nigerian corporate entity is condition precedent for the grant of Oil Mining Lease. As with many other types of commercial leases across the world, oil mining leases require the insertion of operative default[2] clauses that permits the Lessor to oblige the Lessee to unambiguously implement the commitments and express provisions in the lease instrument. The default clauses largely presents the procedure for cessation and dislodgment of the Lessee's tenancy in the event of a default.[3] Likewise, a default clause do include the provisions requiring payments for overdue royalties, rents, and for the payment of damages in the event of breach of other important facets of the non-monetary obligations contained in the lease

[2] R.W. Bentham, ´Joint operating agreements – default` (1990) 8(1) J.E.R.L. 63; John Waite, ´Contractual forfeiture of joint venture interests: are such clauses enforceable` (1990) 8 Oil & Gas Law & Taxation Review 389-392,

[3] Chris Thorpe, Fundamentals of Upstream Petroleum Agreements (CP Thorpe, UK 2008) 141; Peter Roberts, Joint Operating Agreements: A Practical Guide (Globe Law Business, London 2010) 185-204

instrument.[4] The ultimate use of the default clauses are to safeguard the mineral interest owner against possible violations by the lessee. The default clause acts as a trigger mechanism for commencement of action to restore the *status quo*. In Nigeria, a typical example of the default clause is contained in Paragraph 36(b) of the First Schedule of the Petroleum Act,[5] which provides as follows:

> The holder of an oil exploration licence, oil prospecting licence or oil mining lease shall comply with any enactment relating to town or country planning or regulating the construction, alteration, repair or demolition of buildings, or providing for similar matters, which affects him in carrying out the operations authorised by the licence or lease.

Where the lessee is in breach of the default clause, sanctions are invoked by way of penalties. The possible penalties are sometimes included in the contract such as the forfeiture clauses. The foreseeability of the occurrence of penalty gave rise to the introduction of legal rules governing the extent and utility of such penalties.

1.1 THE ORIGIN AND EFFECTS OF PENALTY RULE ON OML OWNERS

Generally, punitive actions are acceptable as a means of injuring a party to a contract where there is substantial breach of the express terms. In this regard, punishment could comprise of charge-backs, cancellation of contract and several other actions intended to motivate the defaulting party to remedy the problem. What makes it punitive is that, the courts usually award damages in

[4] Scott Styles, ´Joint Operating Agreements` in John Paterson, Greg Gordon (eds), Oil and Gas Law: Current Practice and Emerging Trends (DUP, Dundee 2007) 289.

[5] CAP P10 LFN 2004

the sum that is significantly higher than the quantifiable value of the injury suffered by the non-defaulting party. The rationale is that, the damages are designed to punish the defaulting party for irresponsible or reprehensible conduct.

Drakes and Rickard[6] explains that the penalty rule was first used in the 16th Century AD and that, it was necessitated by quest by the courts to avert fraudulent and reckless exploitation in that era because credit facilities were uncommon and debtors were very susceptible. Basically, the penalty was introduced as payment of money specified in the contract and was unenforceable against the offending party where it was an inflated substitute to common law remedies. Simply put, where the creditor is likely to be awarded smaller award by the court for the same breach, the penalty value which is outrageously higher cannot be enforced against the defaulting debtor. In *Dunlop Pneumatic Tyre Co Ltd v New Garage & Motor Co. Ltd (Dunlop)*[7] the court distinguished between the *penalty clauses* and *limited damages clauses*. The general is that, penalty clauses are unenforceable and the limited (liquidated damages are enforceable). Taking this into account, the court succinctly explained that:

(a) Irrespective of the intention of the contracting parties for the use of the words “penalty” or “liquidated damages”, such use of expression is not construed as conclusive. That, it is the duty of the court to find out whether the payment specified is in reality a penalty or liquidated damages.[8]

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[6] Gordon Drakes and Tim Rickard. Important Changes to the English law rule on penalty clauses – what does it mean for franchising? 25 Feb 2016, at https://www.fieldfisher.com › accessed 21 September 2019

[7] [1915] A.C. 847

[8] All Answers ltd, '*Dunlop v New Garage* Case Summary' (Lawteacher.net, September 2019) https://www.lawteacher.net/cases/dunlop-v-new-garage.php?vref=1> accessed 21 September 2019

(b) The crux of a penalty is that it is a payment of money postulated as a legal threat to the aberrant party meaning that, liquidated damage is honest covenanted pre-estimate of foreseeable damage.[9]

(c) The question as to whether the sum of money stipulated is penalty or liquidated damage is a matter of *construction* which should be decided upon the terms and intrinsic settings of each precise contract, adjudged of as at the time of entering into the contract, not as of the time of the breach of the contract.[10] Legal construction in this regard can be propelled by the execution of standardised legal tests as follows:

(i) *The Extravagant test*: The question to be answered is whether the sum of money specified is excessive and reprehensible in amount in association with the highest loss that could possibly be shown to have resulted from the breach.

(ii) *The Greater Sum test:* Is the sum of money specified greater than the sum which ought to have been paid? If yes, then, it is penalty and not enforceable.

The court in the case of *Dunlop* expressly declared that the most crucial ingredient to decipher is "whether the impugned provision is a secondary obligation which imposes a detriment on the contract breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation."[11] Consequently, it will not be considered as penalty if the stipulated sum is the actual estimation of the damage caused.

[9] See: *Clydebank Engineering and Shipbuilding Co Ltd v Don Jose Ramos Yzquierdo y Castaneda* [1905] AC 6

[10] [n. 10]; Also in *Public Works Commissioner v. Hills* [1906] AC 368; *Webster v. Bosanquet* [1912] AC 394

[11] At paragraph 32 of the Judgment. The court further added that: "The innocent party can have no proper interest in simply punishing the defaulter. His interest is in performance or in some appropriate alternative to performance. In the case of a straightforward damages clause, that interest will rarely extend beyond compensation for the breach, and we therefore expect that Lord Dunedin's four tests would usually be perfectly adequate to determine its validity. But compensation is not necessarily the only legitimate interest that the innocent party may have in the performance of the defaulter's primary obligations."

Therefore, the magnitudes of the breach is such that no reasonable person can possibly pre-estimate the real sum of the damage, it will not be regarded as penalty.

Penalty rules predominantly regulate contractual remedies originating from the breach of the express terms of the oil mining lease contract.[12] It is noteworthy, that penalty rules could control the available remedies for breach of secondary obligations such as the obligation to make payments such as royalty.[13] What makes a secondary obligation penal was explained in *Jobson v Johnson*[14] as follows:

> The real question when a contractual provision is challenged as a penalty is whether it is penal, not whether it is a pre-estimate of loss. These are not natural opposites or mutually exclusive categories. A damages clause may be neither or both. The fact that the clause is not a pre-estimate of loss does not therefore, at any rate without more, mean that it is penal. To describe it as a deterrent (or, to use the Latin equivalent, *in terrorem*) does not add anything. A deterrent provision in a contract is simply one species of provision designed to influence the conduct of the party potentially affected. It is no different in this

[12] See: *Jobson v Johnson* [1989] 1 WLR 1026 where it was decided that decided that a clause that offended the rule against penalties could not be enforced and, as such, could not be 'partly enforceable'.

[13] Landmarks of a Century in Oil and Gas Law, Oil, (Gas and Energy Resources Law Section of the State Bar of Texas, 2017)

[14] [1989] 1 WLR 1026. It was also stated that: "'What is necessary in each case is to consider, first, whether any (and if so what) legitimate business interest is served and protected by the clause, and, second, whether, assuming such an interest to exist, the provision made for the interest is nevertheless in the circumstances extravagant, exorbitant or unconscionable. In judging what is extravagant, exorbitant or unconscionable, I consider … that the extent to which the parties were negotiating at arm's length on the basis of legal advice and had every opportunity to appreciate what they were agreeing must at least be a relevant factor." Per Lord Mance.

respect from a contractual inducement. Neither is it inherently penal or contrary to the policy of the law.

Penalty rules cannot regulate a primary obligation such as the obligation to take plug an oil well.[15] In *Cavendish Square Holding B.V v Talal El Makdessi,*[16] it was held that a primary obligation which borders on *price adjustment clause*, could not be enforced by way of penalty and under the penalty rule. In order to determine the probative value of the penalty rules, *true test* is often invoked. The *true test* involves the following determinative variables: (a) the time the contract was made; (b) the non-defaulting party's legitimate interest (financial or otherwise) in contractual performance by the defaulting party; and (b) whether the remedy for breach is excessive or reprehensible in view of legitimate interest.[17]

According to Dann *et. al.,*[18] there are possible arguable defences by which the defaulting party can use as to reducing or excluding liability as follows: "That it constitutes an unenforceable penalty clause; If the penalty argument fails, by arguing that it is entitled to relief against forfeiture. This is because relief against forfeitures would require the defaulting party to cure its breach; something which, where the JOA forfeiture clause applies, it would already have had opportunity to do and would have failed to do. Accordingly, taking account of the likely financial capability of the defaulting party, there may be little scope for relief against forfeiture in the JOA context."[19]

15 Ibp Usa, Kuwait Oil and Gas Exploration Laws and Regulation Handbook. International Business Publications, USA; (January 1, 2009); Susan L. Sakmar, Energy for the 21st Century: Opportunities and Challenges for Liquefied Natural Gas (LNG) (New Horizons in Environmental and Energy Law series, Edward Elgar Pub July 31, 2013)

16 [2015] UKSC 67

17 Adam Dann; Segun Osuntokun; Tim Sumner; Lisa Allenden, Oil & Gas JOA Defaults: Enforcing Forfeiture Clauses after the Cavendish Square Decision. Berwin Leighton Paisner PLP. Online at: www.blplaw.com accessed 19th September 2019.

18 ibid

19 ibid

1.2 THE LEGAL EFFECTS OF DEFAULT CLAUSES AND PENALTY RULES

Default clause functions in such a way that the defaulting party in the contract may not lose all his interest in that he, the defaulter could keep some aspects, the part he may retain are usually weighed on the basis of his overall monetary contributions associated with the total equity of the joint venture undertakings.[20] The benefit is that the default clause may not operate as penalty clause.[21]

In *Jobson v Johnson*[22] it was stated that: "Modern contracts contain a very great variety of contingent obligations. Many of them are contingent on the way that the parties choose to perform the contract. … The potential assimilation of all of these to clauses imposing penal remedies for breach of contract would represent the expansion of the Courts' supervisory jurisdiction into a new territory of uncertain boundaries, which has hitherto been treated as wholly governed by mutual agreement."[23] Drake and Rickard,[24] summed up the effects of the current legal positions that: (a) It is not obligatory for the penalty to give a frank pre-estimate of loss he suffered; (b) The party hoping on the penalty clause should not suffer the consequence of a breach; (c) The main aim of a contractual clause may be to create deterrence against a specific type of breach; and, that, the penalty does not just have to be a specified financial amount. He can withhold or postponed consideration by requiring the transfer of certain properties as the consequence for breach; and, that the contracting parties have a greater freedom to contract for the consequences for breach.

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[20] Eduardo G. Pereira, Encyclopaedia of Oil and Gas Law: Upstream (Volume 1) (New York: Globe Law And Business, 2014)

[21] Eduardo Pereira. Protection against Default in Long Term Petroleum Joint Ventures. WPM 47: Oxford Institute for Energy Studies, 2012.

[22] *Supra*

[23] Cited in Bob Palmer. Annual Review of developments in English oil and gas law 2016. Online at: www.cms-cmck.com accessed 19th September 2019

[24] [n. 8]

1.3 THE IMPLICATIONS OF PENALTY RULES IN THE PETROLEUM SECTOR

The starting point of this segment is to clarify that the larger proportion of disputes arising from oil and gas contractual undertakings are settle at arbitration. However, this does not preclude the applicability of legal rules with respect to the penalty rules. For example, in *Oyeneyin v. Akinkugbe*[25] the court upholds that penalty clauses are contractual provisions that measures against the defaulter, extremely high monetary charges unconnected with the actual breach and therefore unenforceable in Nigeria. This position of the law runs contrary to the practice of forfeiture of the interest clause which are often entrenched in the oil and gas contracts in Nigeria. Unfortunately, forfeiture (Penalty) clauses are integral part of international joint venture agreements within the petroleum sectors.[26]

In Nigeria, joint venture agreements in oil and gas is statutory. Paragraph 35 of the First Schedule of the Petroleum Act[27] gives the Minister of Petroleum the power to impose terms on OELs, OPLs, and/or OMLs thus: "If he considers it to be in the public interest, the Minister may impose on a licence or lease to which this Schedule applies special terms and conditions not inconsistent with this Act including (without prejudice to the generality of the foregoing) terms and conditions as to —

(a) Participation by the Federal Government in the venture to which the licence or lease relates, on terms to be negotiated between the Minister and the applicant for the licence or lease; and
(b) special provisions applying to any natural gas discovered, which provisions shall include—

[25] [2010] 4 NWLR (Pt. 1184) 265
[26] Philip Loots and Donald Charrett, The Application of Contracts in Developing Offshore Oil and Gas Projects (Informa Law from Routledge; 1st edition (March 14, 2019).
[27] CAP P10 LFN 2004

(i) the right of the Federal Government to take natural gas produced with crude oil by the licensee or lessee free of cost at the flare or at an agreed cost and without payment of royalty;

(ii) the obligation of the licensee or lessee to obtain the approval of the Federal Government as to the price at which natural gas produced by the licensee or lessee (and not taken by the Federal Government) is sold; and

(iii) a requirement for the payment by the licensee or lessee of royalty on natural gas produced and sold."

From the provisions of Paragraph 35(a) of the 1st Schedule of the Petroleum Act, it is obligatory for the Minister of Petroleum and the oil company to negotiate the terms and conditions for the OPL license or the OML lease including the entering into joint venture agreements. The bulk of the forfeiture under the JVAs revolve around financial obligations.

Where a financial default is not alleviated within a specified timeframe, the aggrieved party may commence actions to forfeit the interest of the defaulting party in the assets in compliance with the express provisions of the petroleum and related contract instrument. If penalty rule are unenforceable in Nigeria, why are the forfeiture and termination of interest allowed? The answer to this question seems to reside in the originating mode of the oil and gas contract, especially, the Joint Venture Agreements (JVA).[28] Almost all joint venture agreements within the petroleum sectors adopt the Model Form of the international organisations such as that of the Association of International

[28] Kato Gogo Kingston, Pollution and Environmental Responsibility in Petroleum Extraction: in the Niger Delta of Nigeria: Modeling the Coase Theorem. LAP LAMBERT Academic Publishing (October 3, 2017); Greg Gordon, John Paterson, Emre Usenmez, UK Oil and Gas Law: Current Practice and Emerging Trends: Volume II: Commercial and Contract Law Issues Edinburgh University Press; 3rd edition (March 1, 2018); Sandy Shaw, ´Joint Operating Agreements` in Martyn R. David, Upstream Oil and Gas Agreements (Sweet and Maxwell, London 1996) 24–25.

Petroleum Negotiators (AIPN).[29] The Model forms provides for the defaulting party in a JVA's production entitlements are allotted to non-defaulting JVA partner in the event that the default is not remedied within a pre-stated timeframe.[30] For example, Article 8.1 of the Model Form deals with default and notice and provides *inter alia*:

> Any Party that fails to pay when due its Participating Interest share of Joint Account expenses, including cash advances and interest, shall be in default under this Agreement (a "Defaulting Party"). Operator, or any non-defaulting Party in the case Operator is the Defaulting Party, shall promptly give notice of such default to the Defaulting Party and each of the non-defaulting Parties (the "Default Notice")…[31]

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[29] William Hughes, Fundamentals of Oil & Gas Law (PennWell Corp. October 31, 2016); Kato Gogo Kingston, Oil and Gas Laws: A Guide for International Practitioners: Second Edition (LAP LAMBERT Academic Publishing (October 5, 2018)

[30] Scott Styles, ´Joint Operating Agreements` in John Paterson, Greg Gordon (eds), *Oil and Gas Law: Current Practice and Emerging Trends* (DUP, Dundee 2007) 289.

[31] To give effect to the enforcement of Article 8.1, Article 8.4 provides the remedies as follows: "(a) During the continuance of a default, the Defaulting Party shall not have a right to its Entitlement, which shall vest in and be the property of the non-defaulting Parties. Operator (or the notifying Party if Operator is a Defaulting Party) shall be authorized to sell such Entitlement in an arm's-length sale on terms that are commercially reasonable under the circumstances and, after deducting all costs, charges and expenses incurred in connection with such sale, pay the net proceeds to the non-defaulting Parties in proportion to the amounts they are owed by the Defaulting Party hereunder (and apply such net proceeds toward the establishment of a reserve fund under Article 8.4(c), if applicable) until all such amounts are recovered and such reserve fund is established. Any surplus remaining shall be paid to the Defaulting Party, and any deficiency shall remain a debt due from the Defaulting Party to the non-defaulting Parties. When making sales under this Article 8.4(A), the non-defaulting Parties shall have no obligation to share any existing market or obtain a price equal to the price at which their own production is sold; (B) If Operator disposes of any Joint Property or any other credit or adjustment is made to the Joint Account while a Party is in default, Operator (or the notifying Party if Operator is a Defaulting Party) shall be entitled to apply the Defaulting Party's Participating Interest share of the proceeds of such disposal, credit or adjustment against all amounts owing by the Defaulting Party to the non-defaulting Parties hereunder (and toward the establishment of a reserve fund under Article 8.4(c), if applicable). Any surplus remaining shall be paid to the Defaulting Party, and any deficiency shall remain a debt due from the Defaulting Party to the non-defaulting Parties; (C) The non-defaulting Parties shall be entitled to apply proceeds received under Articles 8.4(a) and 8.4(a) toward the creation of a reserve fund in an amount equal to the Defaulting Party's Participating Interest share of (i) the estimated

The "default clause" of the Model Form of the Association of International Petroleum Negotiators ("AIPN") for Joint Venture Agreements further provide that the defaulting party could be required to forfeit its participating interest under the contract to the non-defaulting party, without any compensation, if it fails to pay the monetary obligations as at when due.[32]

The effects of forfeiture clauses in Nigeria's oil and gas JVAs are no doubt punitive in nature. Despite the portentous presence in JVAs, Nigeria petroleum legislation strengthens forfeiture with regards to marginal fields, abandonment of crude oil facilities and farm-out. It is disheartening for the oil and gas investor to go through the strenuous bidding and licensing process and, lose their assets by way of forfeiture for breach of secondary obligations. Typically, the stressful process of licensing cost money, time and efforts.

1.4 THE EFFECTS OF FORFEITURE ON OML, MARGINAL FIELDS, ABANDONMENT AND FARMOUT

In view of the foregoing analysis, it is evidently clear that the ostensibly habitual exercise of unilateral annulment, revoking or terminating the petroleum contracts through forfeiture route is no longer acceptable because it violates international best practices of the oil and gas sectors. Nigeria's Petroleum Amendment Act 1996 introduced paragraph 16A into the First Schedule to the Petroleum Act. Paragraph 16A of the amended Petroleum Act provides as follows:

cost to abandon any wells and other property in which the Defaulting Party participated, (ii) the estimated cost of severance benefits for local employees upon cessation of operations and (iii) any other identifiable costs that the non-defaulting Parties anticipate will be incurred in connection with the cessation of operations."

[32] The Model Clause states as follows: "If a Defaulting Party fails to fully remedy all its defaults by the thirtieth (30th) Day following the date of the Default Notice, then, without prejudice to any other rights available to each non-defaulting Party to recover its portion of the Total Amount in Default, each non-defaulting Party shall have the option, exercisable at any time thereafter during the Default Period, to require that the Defaulting Party completely withdraw from this Agreement and the Contract."

> (1) The holder of an oil mining lease may, with the consent of and on such terms and conditions as may be approved by the President, farm-out any marginal field which lies within the leased area; (2) The President may cause the farm-out of a marginal field if the marginal field has been left unattended for a period of not less than 10 years from the date of the first discovery of the marginal field; (3)The President shall not give his consent to a farm-out or cause the farm – out of a marginal field unless he is satisfied –
> (a) that it is in the public interest so to do, and in addition, in the case of a non- producing field, that the marginal field has been left unattended for an unreasonable time, not being less than 10 years; and (b) that the parties to the farm-out are in all respect acceptable to the Federal Government."

In the event that a marginal field is farmed out, *letter of award* is usually given to the farmee or *farm-out agreement* is executed by the parties. The letter of award grants title over the marginal field to the farmee. Amongst others, there is a mandatory fee to be paid by the farmee known as *Signature Bonus*, it must be paid within 90 days from the date of the award, failure which, the allocation of the marginal field is likely to be revoked.

By the authority of *Talal El Makdessi v. Cavendish Square Holdings BV, Team Y & R Holdings Hong Kong Ltd,*[33] Nigeria's laws on marginal field, abandonment and farm-out are punitive in nature therefore, should be unenforceable[34] in

[33] [2013] EWCA Civ

[34] Anthony Jennings, Oil and Gas Exploration Contracts (2nd edn Sweet & Maxwell, London 2008) 25.

circumstances where the marginal fields are part of the JVA. In *Makdessi's*[35] the rule against penalties applies equally to any form of forfeiture if from the nature and application of it, there is evidence to show that it is penal in nature.[36]

It is not only the marginal fields that can be lost by the OML holder. Paragraphs 23, 24 and 25 of the first schedule of the Petroleum Act, empowers the Minister of petroleum to revoke OEL, OPL and OML where certain conditions are violated by the leaseholder. Paragraph 26 of the same schedule obligates the Petroleum Minister to "inform the licensee or lessee of the grounds on which the revocation is contemplated and shall invite the licensee or lessee to make any explanation if he so desires." It is important to observe that the said Petroleum Act was enacted in 1969, some of the provisions have outlived their usefulness. Therefore, the rickety powers of the Petroleum Minister to unilaterally revoke OEL. OPL and OML as enshrined in the said legislation are contrary to the penalty rules hence, can be overturned in competent courts of law.

Despite the weak legal fulcrum of the revocation powers of the Petroleum Minister, in June 2019, seven oil block licenses were revoked in Nigeria, for violation of what was described as "*legacy debts*."[37] The unilateral revocation were published in a statement by the Department of Petroleum Resources (DPR) *inter alia*:

> Notice is hereby given that in furtherance of the presidential directive on the recovery of legacy debts owed the Federation and in line with the provisions of the

[35] ibid
[36] Bernard. G. Taverne, *Co-Operative Agreements in the Extractive Petroleum Industry* (Kluwer Law International, The Hague 1996) 55.
[37] Legacy debts were described as consisting of rents, royalties and taxes.

> Petroleum Act Cap. P10LFN 2004, the under listed Oil Mining Leases and Oil Prospecting Licence have been revoked by the Federal Government of Nigeria for non-compliance with statutory regulatory obligations.[38]

The legacy debts were secondary obligations hence, violated the penalty rules.[39] The affected licenses are OML 98,[40] OML 120 and OML 121,[41] OML 108,[42] OML 141,[43] OML 110,[44] and OPL 206.[45] In addition to the revocation being contrary to the penalty rules, it overstepped the doctrine of "due process" and the doctrine of "natural justice" enshrined in Section 36(5) and section 44(1) 1999 of the Constitution (as amended). The Constitutional provisions provides for fair hearing on matters of individuals' civil rights and civil obligations.[46]

In 2009, Nigeria revoked the OPL321 and OPL323 held by Korea National Oil Corporation (KNOC) for breach of monetary obligations. KNOC successfully challenged the revocation and obtained an injunction restraining the Federal Government from acting on its revocation order. However, the government got a stay of execution of the injunction and went ahead to seize

[38] Legacy debts: FG revokes five companies' oil block licences, June 7, 2019. Online at: https://punchng.com/legacy-debts-fg-revokes-five-companies-oil-block-licences/

[39] Nigerian petroleum regulator revokes six oil block licences (Reuters, June 6, 2019) Online at: www.reuters.com accessed 24 September 2019

[40] Held by Pan Ocean

[41] Held by Allied Energy (Erin Energy), the company shortly applied for bankruptcy

[42] Held by Express Petroleum. The technical activities were managed by Shebah Exploration & Petroleum, under the parenthood of Seplat

[43] Held by Emerald Resources

[44] Held by Cavendish Petroleum Nigeria

[45] Held by Summit Oil International

[46] *Osho v. Foreign Fin. Corp.* (1991) 4 NWLR (Pt. 184)157. 2, (1991*); Dantsoho v Mohammed* [2003] 6 NWLR (pt 817) 457 SC.; *Obikoya v Governor of Lagos State* [1987] 1 NWLR (pt 50) 385 CA; *Ibrahim v Mohammed* [2003] 6 NWLR (pt 817) 615 SC; *Ereku v Military Governor Mid-Western State of Nigeria and Others* [1974] 10 SC 42; *CSS Bookshops Ltd v RTMCRS* [2006] 11 NWLR (pt 992) 530 SC; *Peenock Investments Ltd v Hotel Presidential Ltd* [1983] 4 NCLR 122; *Alhaji Bello v Diocesan Synod of Lagos* [1973] 1 All NLR (pt 1) 247; *Nigerian Telecommunications Ltd v Chief Ogunbiyi* [1992] 7 NWLR (pt 255) 543;

and re-assign the licenses. Vines *et. al.,* summed up thus: "This saga illustrates both how poorly Nigeria manages relations with its business partners and how political considerations interfere with commercial decisions in the vital oil industry."[47]

2. SOCIAL EFFICIENT SOLUTIONS TO THE HOST COMMUNITIES' CONCERN

2.1 COMMUNITY LAND RIGHTS – SURFACE INTEREST

The concept of private property ownership is central to modern democratic society. Generally, in property law, ownership of property usually consist of the 'bundle of legal and equitable rights'. The bundle of such rights include the owner's right to use and enjoy the property, the right to sell or rent the property to others, and the right to exclude others from using or interfering with the property.[48]

In order to be able to enforce the rights to safe and healthy environment, there has to be the existence of some form of ownership or possessory rights over the acreage to which the rights accrues. In essence, it is practically impossible to enforce environmental safety rights against any polluter in the absence of the existence of the rights to the land, sea and air. For any environmental safety action to succeed, the possessory or ownership rights over the polluted lands must not be extinguished before the occurrence of the pollution.

With regards to the development and exploitation of crude oil and natural gas in Nigeria, and the resulting environmental consequences, two issues must be

[47] Alex Vines, Lillian Wong, Markus Weimer and Indira Campos. Thirst for African Oil Asian National Oil Companies in Nigeria and Angola. A Chatham House Report, 2009. Online at: https://www.chathamhouse.org/sites/default/files/r0809_africanoil.pdf accessed 24 September 2019

[48] Kato Gogo Kingston & Samuel Chisa Dike (2019) The Accommodation Doctrine and The Compulsory Acquisition of Lands for Oil and Gas Projects in Nigeria. Prime Journal of Advanced Legal Studies Volume 9 Number 1

differentiated. The first is the ownership of crude oil and natural gas. The second is the ownership of the surface of the lands where the crude oil and natural gases are being extracted. Both issues have significant but complicated legal implications with regards to the preservation of the environment.[49]

The first issue revolves on the pivotal strand of the theory of eminent domain. The theory states that the government or the monarch of a country can compulsorily take private lands for public use with or without compensation. For the government to successfully acquire the rights to the lands of private persons and communities, it must back its 'taking' by enacting coercive legislation to prevent the former private land owners from enforcing their land rights against the government and against the oil companies.[50]

The Federal Government of Nigeria enacted coercive statutes that empowers it (the eminent domain) to forcefully acquire the ownership rights of all minerals in the country. The laws are: The Land Use Act 1978;[51] The Constitution Federal Republic of Nigeria 1999 (as amended);[52] The Exclusive Economic Zone Act 1978;[53] and, The Petroleum Act.[54] With respect to the

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[49] Kato Gogo Kingston (2018) Oil and Gas Laws: A Guide for International Practitioners (Second Edition) (Mauritius: Lambert Academic Publishing).

[50] The implication of this theory is that, the government can enact coercive legislation to back its desire to seize any land from private persons for any purpose it may classify as public good.

[51] Section 1 vest all lands in the governor of each state. Section 28(1) of the Land Use Act 1978 states the "it shall be lawful for the Governor to revoke a right of occupancy for overriding public interest."

[52] Section 44(3) states: "…. 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 rest in the Government of the Federation and shall be managed in such manner as may be prescribed by the National Assembly."

[53] Section 2(1) "…. sovereignty and exclusive rights with respect to the of exploration and exploitation of the natural resources of the seabed, subsoil and superjacent waters of the Exclusive economic Zone shall vest in the Federal Republic of Nigeria and such rights shall be exercised by the Federal Government……"

[54] Section 1 provides as follows: "… to the effect that the entire ownership and control of all petroleum in, under or upon any lands, including and covered by water) which is: (a) is in Nigeria or (b) is under the territorial waters of Nigeria, (c) forms part of the continental shelf; or (d) forms part of the Exclusive Economic Zone of Nigeria."

ownership of crude oil and gases that are within the offshore zones, Nigeria acceded to the United Nations Convention on the Law of the Sea (UNCLOS) 1982.[55] In view of the preceding explanations, it is not in doubt that the Federal Government of Nigeria is the legal owner of all the minerals in Nigeria including the minerals that are situated within its maritime zone.

The second issue centres on surface ownership of land, surface use, reckless use (including pollution) and the rights to seek redress. It must be highlighted that rights of the legitimate surface occupier or surface owner of land are enshrined in customary international law under the general concept of *accommodation doctrine*, now fully entrenched in oil and gas law.

The canon of accommodation doctrine evolves from the theory of *due regard.* Accommodation doctrine is also known as the principle of '*alternative means.*'[56] The doctrine denotes that, irrespective of the fact that the owner or holder of the surface of the land may not be the owner of the crude oil or other minerals underneath the land, he has the right to protect the surface and any violation of his surface right attracts remedies in law. For example, in Nigeria, Section 44(3) of the Constitution FRN 1999 (as amended); Section 2(1) Exclusive Economic Zone Act 1978; and, Section 1 Petroleum Act[57] firmly placed all the minerals in Nigeria under the ownership and control of the Federal Republic of Nigeria. For this reason, the Federal Government may transfer or assign some aspects of such rights to the oil companies by way of licences (concessions).

[55] Article 77 (1) of the United Nations conference on the law of the sea (UNCLOS) 1982 provides that the coastal sovereign state has ownership, control and development of natural resources in the exclusive economic Zone.(Which Nigeria became a party of in 1986), this rights are prevented from extending to interfere with the territory and territorial rights of neighbouring states.

[56] [n 1]

[57] CAP P10 LFN 2004

The oil companies therefore become the minerals lease holders. There is thus, an implied rule that the oil companies have automatic easements (the right of way) allowing them to gain access to the crude oil by passing through the surface of the lands that are occupied or owned by private persons and communities. Hence, the oil firms must *reasonably accommodate* the private surface owners' rights. This implies that the oil firms are obliged to act in such manners that they should satisfactory accord due regards to the surface rights owners.

In some instances, such due regards may include but not limited to making adequate plans for the relocation of the surface rights owners by providing alternative arrangements such as the provision of alternative accommodation.[58] Due regards also require that the oil firms should use alternative routes to gain access to their project sites to minimise interference with the surface occupation of persons and communities. It also involves making adequate plans to compensate the land surface owners where the use of the surface has caused damages or hardship.

The utility of accommodation doctrine was prominently explained in *Getty Oil Company v. Jones*.[59] In that case, the cause of action was that, Jones sought remedy from Getty for negligently violating his accommodation doctrine in that Getty installed a very high oil pumps in the boundary of Jones' property which obstructed the water sprinkler system of Jones to the effect that Jones could not supply water to his own property, which consequently affected Jones crops.[60] The Supreme Court of Texas decided that Jones was entitled to peaceful enjoyment of the surface of his land which otherwise was

[58] This happens where there is a foreseeable chance that the exploitation of crude oil will cause significant disruption to the lives and properties of the surface dwellers. In such instances, the oil companies are obliged under this principle to pay compensation as well as make provision for the resettlement of the communities/persons.

[59] 470 S.W.2d 618 (Tex. 1971)

[60] [n. 11]

impeded by Getty Oil. The court further said that, Getty Oil ought to have reasonably accommodated the rights and concerns of Jones. Therefore, Jones rights over the surface of the land were violated by Getty Oil notwithstanding that Getty Oil was the minerals interest owner.[61] Irrefutably, the court made it clear that, "the rights implied in favour of the mineral estate are to be exercised with due regard to the rights of the owner of the *servient* estate."[62] This simply mean that the mineral right owners[63] should reasonably accommodate the surface owners in the following circumstances:

a) When there is an existing use of the surface prior to the acquisition of the mineral mining license;
b) Where the mineral owners' use of the surface impedes or harms the existing use of the surface to the detriment of the surface rights owners; and
c) Where it is within the recognised minerals industry practices, that there are available alternatives means by which the mineral license owners could use to recover the minerals without interfering with the surface owners' rights.[64]

In the case of *Buffalo Mining Co. v. Martin*,[65] it was decided that the mineral interest owners must exercise care and use proper skills which are "reasonably necessary for the extraction of the mineral" and "without substantial burden to the surface owner." In the same direction, in *Chartiers Block Coal Co., v. Mellon*[66] where the court was confronted with decision as to the applicability of accommodation doctrine on multiple mineral interest owners. The court reached the decision that, "… against the owner[s] of the surface each of the

[61] *Haupt Inc. v. Tarrant County Water,* 870 S.W.2d 350 (Tex. App. Waco 1994)
[62] [n. 11]
[63] This refers to the oil companies that have subsisting mineral lease licences.
[64] [n. 11]
[65] 267 S.E.2d 721 (W.Va. 1980)
[66] 152 Pa 286, 25 A 597 (1893)

several purchasers would have the right...to go upon the surface to open by way of shaft, or drift or well, to his underlying estate..." This decision reiterates the willingness of the court to enforce the rights of the surface owners against the reckless mineral right holders. This is because: "when the soil belongs to one person and the mine another, the right to work the mine carries with it the use of so much of the surface as is strictly necessary and reasonable."[67]

In this circumstance, it is important to explain the legal concept of reasonableness. In *Associated Provincial Picture Houses Ltd. v Wednesbury Corporation*[68] the English Supreme Court explained that an action of a private or public entity is construed as unreasonable "if it is so unreasonable that no reasonable person acting reasonably could have made it." To triumph on a claim under the accommodation doctrine the surface rights owner must prove two things as follows:

(a) That the oil company's use of the surface totally impedes or considerably damages the existing surface use, and
(b) That the surface owners have no reasonable alternative method available to continue their existing use of the surface alongside the reckless use and/or damages by the oil company.

The claimant (surface owner) must also show that under the circumstances, that there are alternative reasonable, customary, and industry-accepted methods that are available to the oil company which ought to have been used by the oil company to extract crude oil without interfering with the surface owners existing use of the surface. Honestly, what this means is that, the claimant have to put up a convincing argument to show that, the damages to

[67] *Dewey v. Great Lakes Coal Co* 84 A. 913 (Pa. 1912)
[68] [1948] 1 KB 223

the surface of the lands could have been avoided *but for* the wilful negligence and recklessness of the oil company.

The *but for test* was further developed in *Merriman v. XTO Energy, Inc.*,[69] in which the court laid out the requirements for proof of violation of the accommodation doctrine. To prove breach of the accommodation doctrine, the surface owner must first show that:

a) That the oil firm's use of the surface of the land of the claimant completely precludes or substantially impairs the existing use. This means that, the oil company recklessly and negligently use of the surface thereby causing harm to the claimant;
b) That the oil company did not show that there were no reasonable, customary, and industry-accepted methods available to the oil company that would have allowed the recovery of crude oil and also allow the surface owner to continue the existing use. This means that the claimant need to show that there were other rational options by which the defendant ought to have adopted in the course of the conduct of the oil production activities in the project location.

Furthermore, in *Amoco Production Co. v. Carter Farms*,[70] the court found that the defendants were in violation of accommodation doctrine in that they recklessly neglected the due regards of the claimant's surface rights hence, they were liable to pay substantial damages to the claimants. By the same token, in *Hunt Oil Co. v. Kerbaugh*,[71] the court decided *inter alia*:

> …the owner of the mineral estate must have due regard for the rights of the surface owner and is required to exercise that degree of care and use which is a just consideration for the rights of the surface owner…

[69] 407 S.W.3d 244 (2013)
[70] 703 P.2d 894 (N.M. 1985)
[71] 283 N.W.2d 131 (N.D. 1979)

The same outcome was reach in other notable cases such as the case of *Flying Diamond Corp. v. Rust*,[72] where the court explicitly stated that both the mineral rights[73] owner and the surface occupier/owner have the rights to use and enjoy their properties without interference. In *Diamond Shamrock Corp. v. Phillips*,[74] the court decided that the "mineral owner must make reasonable usage of the surface and is liable for damages caused by any unreasonable use." In *Buffalo Mining Co. v. Martin*,[75] the court affirmed that the mineral owner's use of the land surface must be "reasonably necessary for the extraction of the mineral" and "without substantial burden to the surface owner."[76]

3. SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

3.1 SUMMARY

This analysis is focused on the associated problems of the Oil Mining Lease Number 11 which our State under your able leadership have acquired 45% shares. The goal of the analysis is to highlight the possible problems that may arise in the venture and, to suggest solutions and policy directions to sustain profitability and eliminate foreseeable losses.

Additionally, the analysis explores the social efficient solutions and enumerates the various prospects of the oil and gas undertaking. It acknowledges among other things, that, the Petroleum Act CAP. P10 LFN 2004 expressly provides for the procedure for negotiation between the Federal Government of Nigeria and the oil and gas companies before the

[72] 551 P.2d 509 (Utah 1976)
[73] In Nigeria, the rights are Oil exploration licence; Oil Prospecting Licence and Oil Mining Lease contained in Section 2(1)(a) to 2(1)(c) of the Petroleum Act, respectively.
[74] 511 S.W.2d 160
[75] 267 S.E.2d 721
[76] In *Gillespie v. American Zinc & Chemical* 93 A. 272 (Pa. 1915) the court avowed the grant of an injunction which ordered the well location originally designated by the mineral titleholder. The planned location would have "interfered" with the surface owner's use and development of land.

latter can procure participating interests in any undertaking in which an oil prospecting licence and/or oil mining lease is involved.

Consequently, it is hereby explained that the Federal Government has the statutory authority to exercise the rights of "takings" and "revocation" of oil prospecting licence (OPL) and Oil Mining Lease (OML) for public interest.

Flowing from the capacity of the Federal Government to take and/or revoke any OPL and OML at will, this analytical piece provides, a clear direction by which Rivers State government as a shareholder in OML 11 may wish to adopt to sustain and safeguard her interest thereof. It must be noted that Rivers State ownership of 45% shares in OML 11 is not a guarantee that it will yield sustainable profits to the State. The OML can be revoked by the Federal Government anytime, as a punitive measure. This is the central goal of this expert analysis. Furthermore, it is very important to highlight that paragraph 12(1) of the First Schedule of the Petroleum Act stipulates that ten years after the grant of an oil mining lease, one half of the area of the lease shall be relinquished.

Drawing from the circumstances of the Federal Government revocation of OML 98, OML 120 and OML 121, OML 108, OML 141, OML 110, and OPL 206. This analytical piece argues that, though the Federal Government of Nigeria is entitled to participate in crude oil concessions in view of her ownership of oil and gas assets within Nigerian territory, that, the degree and magnitude of government takings and forfeiture of assets of the oil companies as punitive measure for breach of secondary obligations are unfair and contrary to the rules against penalty. It also argues that, the default clauses and the penalty rules in the JV contracts are often complicated by the unstable legal landscapes.

It recommend amongst others that JV agreements in oil and gas ventures should contain express indemnity clauses designed to protect the oil companies and partners against arbitrary forfeitures. Liabilities flowing from secondary obligations should be capped ab initio in such a way that remedies that exceed the capped value of a breach should be construed as penalty, therefore, void and unenforceable. Notwithstanding the absence of alternative legal framework to protect the shareholders of OML in Nigeria, Rivers State Government should act timely to put mechanism in place to preserve its equity in OML 11.

This analysis further presents the various ways by which the operators of the OML may conduct business without encountering any form of resistance and conflicts with the host communities. Amongst others, it explained the unsustainable and non-functional nature of Memorandum of Understanding which most oil companies have been signing with the host communities.

This analysis further argued that the Oil Companies are not obliged to respect and obey the provisions of MOUs because the said instruments lack the fundamental ingredients of contract thus, unenforceable. It supports its argument with the internationally recognised legal doctrine known as the "accommodation doctrine" (also known as the doctrine of due regards). Taking a comparative stance of oil and gas dispute avoidance legal frameworks of some States in the United States of America, the expert recommend the enactment of Rivers State legislation to be known as RIVERS STATE SURFACE USE, DAMAGES AND COMPENSATION LAW. The analysis explores the intricacies and importance of the proposed Act which should replace the current system of MOU and GMOU.

The analysis further provides a nutshell information regarding the complex issue of determination of profit oil and associated partnership shares. It explained that there are several operational expenditure which the operator

ought to provide routine honest and accurate disclosures. However, that, many operators are not very transparent. Consequently, Rivers State as a shareholder should take reasonable steps to prevent possible losses and sustain the profits of her shares in the venture without being 'short-changed'.

In essence, it is recommended that there should be a pragmatic policy direction by Rivers State Government to monitor the OML 11 undertakings and the operation of the fundamentals of the flow of the OML to sustain transparent accounting by the operator. This is because, the risk of not monitoring the operators from the production sources, is likely to give room to inflated declared cost oil and under-declaration of the actual value of profit oil.

Where the operator declares higher value of cost oil, the profit oil to which Rivers State is to receive its share profit will be drastically lower than the actual profits. To circumvent this foreseeable tactics of the oil and gas operating partners, expert knowledge and skills are crucial in interpreting information supplied by the operators including the use of realizable prices in the determination of royalty and petroleum profit taxes. In essence, the bounds for new crude oil streams produced from the OML contract area including the proximate marginal fields should be clearly monitored to determine profitability in accordance with the express clauses of the Joint Venture. The expert monitoring mechanism require an existing or purposefully created State Agency or State Corporation manned by selected experts that has the crucial skills and knowledge of oil and gas operations including skilled oil and gas law experts that must regularly report directly to the Governor.

3.2 CONCLUSIONS

3.2.1 PROTECTING THE HOST COMMUNITIES TO BOOST OIL PRODUCTION

Despite the provisions of the Land Use Act[77] of Nigeria which created a trust of land in each State of the country by making the State Governors the trustees holding same for the Federal Government, the Land Use Act did not exclude the overall interests of the land surface owners. Nonetheless, in *Kachalla v. Banki,*[78] and in *Ezennah v. Attah,*[79] it was stated that the highest legal rights an individual can acquire over land in Nigeria is the right of occupancy. The restricted right is provided in Section 5(1) of the Land Use Act. Therefore, it is notable that, so far as the right of occupancy of the surface subsist, there is the existence of accommodation doctrine by which breach of same could attract remedies, *ubi jus ibi remedium.*[80]

Notwithstanding that the rights of the occupants and holders of the surface of the lands are protected by the common law maxim of *due regards* (accommodation doctrine), in Nigeria, Paragraph 37 of the First Schedule of the Petroleum Act[81] recognizes the accommodation doctrine as follows:

> "The holder of an oil exploration licence, oil prospecting licence or oil mining lease shall, in addition to any liability for compensation to which he may be subject under any other provision of this Act, be liable to pay fair and adequate compensation for the disturbance of surface or other rights to any person who owns or is in lawful occupation of the licensed or leased lands."

[77] Chapter L5 LFN 2004
[78] (2006) All FWLR (Pt. 309) p. 1420
[79] (2004) All FWLR (Pt. 202) p. 1858 at 1884
[80] Latin maxim meaning, where there is a wrong, there must be a remedy.
[81] CAP P10 LFN 2004

The implication of the common law maxim and the aforesaid provision of the Petroleum Act is that, the host communities of OML 11 are entitled to due regards hence, the operator of the oil facilities are under legal obligation to reasonably accommodate the concerns of the host communities. The use of Memorandum of Understanding (MOU) as an instrument of care is likely to violate these legal benchmarks. The MOU is deceitful, hence has lost its relevance.

3.2.2 FORFEITURE AND REVOCATION OF OML RIGHTS

Earlier in this analysis, efforts have been made to explain how OML rights can be lost to the Federal Government by way of punitive forfeiture. However, not all civil forfeitures are punitive. Civil forfeiture may be legitimate where the laws and regulations of a country adopts it as a means for government to seize criminal assets without filing criminal charges.[82]
Civil asset forfeiture laws empowers governments to seize tangible and intangible assets from persons (including corporate entities) who are suspected of being associated to criminal activity. In civil forfeiture actions the seized properties are reasonably believed to be linked to crime.[83] In essence, forfeiture is more appropriate in criminal violation to create deterrence.

It is unreasonable for contracting parties in oil and gas joint venture to adopt the Model Forms without modifying the clauses to give freedom of contract. Freedom of contract occur when the contracting parties are permitted to decide the express terms and conditions that should be pertinent to their

[82] S. R. Klein, Civil in Rem Forfeiture and Double Jeopardy. Iowa Law Review, Vol. 82, p. 183, 1996. Available at SSRN: https://ssrn.com/abstract=10158 accessed 26 September 2019

[83] See: Civil Asset Forfeiture, online at: http://www.drugpolicy.org/sites/default/files/civil-asset-forfeiture-january2019_0.pdf accessed 26 September 2019

contractual relationship.[84] The chosen clauses should not offend the extant laws (national and international). Additionally, the contracting parties are committed to act in accordance with the principles of probity and good faith, tightly connected with the doctrine of *pacta sunt servanda*.[85]

In the specific context of the oil and gas industry, a party's freedom to choose with whom and on what terms to contract becomes particularly important given the significant investment of time and money intrinsic in exploration and production joint ventures. Because the joint operations cannot stop simply due to lack of funds, the parties will normally need to be as clear and specific as possible in their Joint Operating Agreements ("JOA") in order to discourage and manage any party's payment default.[86]

Investments in the oil and gas sector in Nigeria should ordinarily flow from a planned viewpoint, in accordance with the supporting laws and regulations.[87] Despite the use of punitive forfeitures resulting from the enforcement of default clauses in joint venture contracts, the government has used various reasons to seize oil and gas assets from licence holders since 1969. For example, consecutive national governments have withdrawn crude oil licenses from several upstream petroleum operators. "With due sense of circumspect, when irregularities manifest in the process and the grant of substantive licences, such does not vest in the government an unfettered right to annul the licence. There are evidences of such occurrence in spite of established procedures regulating annulments, commonly referred to as

[84] Leonardo P. Costa, Fernando Fernandes Xavier and Bruno Belchior. Brazil: Enforceability Of The JOA Forfeiture Mechanism Under Brazilian Law,10 June 2014, online at: http://www.mondaq.com accessed 26 September 2019

[85] Latin expression meaning: Agreements must be kept.

[86] ibid

[87] O.A Oyewunmi & O.J Olujobi. Transparency in Nigeria's oil and gas industry: Is policy re-engineering the way out? (2016) International Journal of Energy Economics and Policy,5(4), 630-636.

revocation or cancellation."[88] No matter how the government may wish to defend the legitimacy of its actions, it is counterproductive as it is capable of deterring prospective investors. Recently, the conflicts that arose between Nigeria and Malabu Oil & Gas Limited as a result of the revocation of Oil Prospecting Licence (OPL) 245 resurrected debates with regards to the faulty licensing regime in the oil and gas sector.

In 2017, the Natural Resource Governance Institute (NRGI) undertook a survey of the social efficiency of oil and gas investment in Nigeria and found that, the licensing regime of the industry is the most problematic part of the enterprise. The NRGI further observed that the uncertainty in the licensing regime was partially responsible for the lack of transparency resulting in only 30 percent active production, implying that just 30 percent of the issued licenses were actually in use. The implication is that, the more uncertainties that trails the licensing regime, the more revenue Nigeria is likely to lose. It is also noted that, some of the issued licenses have become subjects of legal actions where the objectivity of the licence award processes have been controversial.

From the preceding discourse, it is evident that the customary liability distribution models often limits the defaulting parties' burden to acts of wilful misconduct.[89] In oil and gas joint venture contracts, there are clauses that allocate indemnity[90] such as the hold harmless provision however, such provisions do not apply in the circumstances of gross negligence.[91] It is argued that, a breach of secondary obligation cannot be construed as gross

[88] Olusola Joshua Olujobi and Olabode Adeleke Oyewunmi. Annulment of Oil Licences in Nigeria's Upstream Petroleum Sector: A Legal Critique of the Costs and Benefits. International Journal of Energy Economics and Policy, 2017, 7(3), 364-369

[89] *Adams Resources Exploration Corporation v Resources Drilling Inc* 761 SW 2d 63

[90] *IP Petroleum Company, Inc. v Wevanco Energy* 116 SW 3d 888

[91] AIPN, 2002 Model Joint Operating Agreement', www.aipn.org accessed 29 September 2019

negligence in the face of other possible reasonable excuses.[92] Therefore, the rule against penalty is valid and should be applicable in Nigeria's oil and gas governance and legal regime.

3.3 RECOMMENDATIONS

3.3.1 SHIELDING AGAINST FEDERAL GOVERNMENT REVOCATION OF OML

a) It is recommended that Rivers State Government should ensure that it plays active role in the administration and governance of all matters concerning OML 11. The compliance mechanism of the Joint Venture with regards to the primary and secondary obligations must never be neglected. In this circumstance, primary obligations include but not limited to the express provisions of the joint venture instrument. The secondary obligations include but not limited to the obligations owed to the Federal Government. The secondary obligations can act as trap by which punitive revocation by which the Federal Government can invoked to end the lifespan of the OML.

b) The State Government should, where and when possible sponsor a Bill in the National Assembly for the review of the relevant laws and policies which empowers the Federal Government to use punitive revocation powers to terminate OPL and OML because such powers are contrary to international law and not in tandem with international best practice of the oil and gas industries.

c) Where forfeiture of assets is unavoidable, proprietary rights should not be removed from a contractual party without appropriate reparation and without equitable consideration. In most cases, the values of the forfeited assets are far more than the actual values of the defaulted monetary sum. There should be a balance to reduce undue losses. The

[92] *Walters v. Whessoe Ltd and Shell Refining Co* Ltd [1968] 2 All ER 816

Joint Venture Agreement of OML 11 should incorporate sufficient clauses in this regard.

d) In order to help parties to avoid controversy, which is particularly strong in countries with a civil law tradition including Nigeria, the new Model Form JOA released by AIPN in 2012 included a number of alternative options to deal with defaults. These options should be carefully chosen by the parties, taking into consideration the laws and practices of Nigeria.[93]

e) Joint venture agreements in the oil and gas sector in Nigeria should contain explicit indemnity clauses designed to protect the partners and including the operators against arbitrary forfeitures.[94] Alternatively, the parties to JV contracts should avail themselves to specific limiting liability clauses which should expressly indicate the total sum payable in the event of breach of secondary obligations. This could provide certainty whereby the clause is designed to create liability cap. It should also be made clear that any remedies that exceeds the capped value of a breach is punitive therefore, void. It will enable the parties to JV contracts to weigh the maximum level of possible losses.

3.3.2 ENACTMENT OF SURFACE USE, DAMAGES AND COMPENSATION LAW

The Rivers State House of Assembly should enact a law to be known as *SURFACE USE, DAMAGES AND COMPENSATION LAW* which should expressly regulate the extent of rights to which the land surface occupiers and holders should exercise proprietary rights to social, health and safety. Without such a law, the possibilities of frequent legal actions challenging the oil firms are very high considering the growing awareness

[93] ibid
[94] *Caledonia (EE) Ltd v Orbit Valve* (1994) 1 WLR 221

about some of the existing rights that are attached to the surface of the lands where oil and gas including other industrial activities are being undertaken.

In ten States of the United States of America (Alaska, North Dakota, Illinois, Montana, Oklahoma, Pennsylvania, South Dakota, Tennessee, Texas, and Wyoming), the controversy of access to minerals lands and the rights of the surface owners have been addressed through enacted State laws. For example, the *Surface Damages Act* in Oklahoma was the basis of the decision of the court in *Schneberger v. Apache Corp.*,[95] where the court stated that, the aim of the Surface Damage Act is to offer suitable reparation to the surface owners for damages resulting from the activities conducted by oil and gas companies. Similarly, in *Compton v. Davis Oil Co.*,[96] the court observed inter alia: "*It cannot be said that the surface of the land constitutes a less vital resource to the State of Oklahoma than does the mineral wealth which underlies it. The surface supports development for business, industrial and residential purposes. It also supports our vital agricultural industry. The passage of the Surface Damages Act guarantees that the development of one industry is not undertaken at the expense of another when the vitality of both is of great consequence to the well-being of our economy.*"

The proposed *SURFACE USE, DAMAGES AND COMPENSATION LAW* is very likely to break the deadlocks of the incessant violence and agitations of the surface owners and communities where oil and gas are being extracted. The law when enacted shall derive credence from the provisions of Paragraph 37 of the First Schedule of the Petroleum Act.[97]

The *SURFACE USE, DAMAGES AND COMPENSATION LAW* should provide the mechanism for maintaining the equilibrium between the oil and gas industry and land surface rights owners. The law also should oblige the

[95] 1994 OK 117, 14, 890 P.2d 847, 853-54.

[96] L. Mark Walker, Note, Oil and Gas: Surface Damages, Operators, and the Oil and Gas Attorney, 36 OKLA. L. REV. 414, 414 (1983).

[97] *Supra*

oil companies to negotiate and enter into written agreements with the land surface owners before drilling begins.

The implication of the proposed legislation is that the oil companies cannot exclude or limit liabilities for any surface damages (including pollution) resulting from any aspect of crude oil exploration and production. The host communities and the oil companies should bargain and enter into a written agreements in advance of the oil companies' actual entry into the lands and prior to the commencement of crude oil development projects.

The legislation should eliminate the current faulty and treachery of non-legal relationship confined in Memorandum of Understanding (MOU). As a matter of fact, the oil firms are not obliged to comply with the provisions of such documents. They simply treat such documents in the same category as the provisions of Corporate Social Responsibility (CSR).

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