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INSIGHTS

Nigerian Marginal Fields: New Bid Round and New Guidelines

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Nigeria's Department of Petroleum Resources ("**DPR**") announced on 1 June 2020 the launch of a new marginal field bid round. Fifty-seven marginal fields have been made available, being a mix of onshore, swamp and shallow-offshore fields. The DPR also released new guidelines covering the bid process, the award and farm-out of marginal fields and their operation ("**Guidelines**"). We consider the essential features of marginal fields – a somewhat complex arrangement of law, regulation and practice – along with the significant requirements of the 2020 bid process and new Guidelines, and the issues that participants, investors and lenders should have in mind.

What is a marginal field?

"Marginal fields" were first established in Nigeria in 1996 in an effort to engender local participation and operation in the oil and gas industry. A marginal field is defined in the Guidelines as a field that has been discovered and left unattended for a period of not less than 10 years from the date of first discovery, or such field as the President of Nigeria may identify. Once designated a marginal field, that area is "farmed-out" from the wider Oil Mining Lease ("**OML**") area. The overall effect is to cede such area/field from the original OML holders to the recipient of the marginal field award (but this arrangement does not establish a new OML for the marginal field).

The first marginal field bid process started in 2001 and resulted in the award of 24 marginal fields to 32 companies. A bid round was scheduled in 2013 but was significantly delayed following the initial announcement and ultimately never concluded. Recently, the DPR has taken steps to revoke previously awarded marginal fields (some of which are being contested but have been included to be freshly awarded in this 2020 bid round).

Key features

Marginal fields are awarded to indigenous companies but often involve farm-in and joint venturing arrangements with international oil companies (within mandatory maximum participation allowances). Historically, these arrangements have involved the provision of technical and financial services to the indigenous oil company, who must be the designated operator of the field.

The award of the marginal fields triggers a farm-out agreement to be made with the original OML holders, which allocates responsibilities and liabilities as between the area holders, as well as the royalty payable and terms for accessing infrastructure.

What are the main terms of the Guidelines?

- **Bidding process:** Interested companies must register for access to a DPR portal and submit an application for pre-qualification. Bidders can then review field-specific data and thereafter submit a detailed technical and commercial bid, and the Guidelines explain the expected contents of such bid and the criteria for evaluation. A selection committee will evaluate and select the winning bids. The parties then proceed to negotiate a farm-out agreement (and, in the event that two or more companies are awarded one field, a joint operating agreement).

- **Eligibility:** The process is open to all indigenous companies that are "wholly or substantially" Nigerian, duly registered to carry out exploration and production operations in Nigeria, and can demonstrate requisite experience and capabilities to develop the field. Companies that are indebted to the Nigerian Government or hold assets that are not being operated in a "business-like manner" will not be eligible.

- **Applicable fees:** Bidders must pay the following fees at various points in the process:
  - Registration fee of five hundred thousand naira.
  - Application fee of two million naira per field (previously two hundred thousand naira).
  - Bid processing fee of three million naira per field (previously three hundred thousand naira).
  - Data prying fee of fifteen thousand US dollars per field (previously three thousand US dollars).
  - Data leasing fee of twenty-five thousand US dollars.

- **Signature bonus**: Companies are expected to confirm their willingness to pay a signature bonus upon selection and prior to the award of the marginal field. The amount of such signature bonus is not disclosed in the Guidelines (but was three hundred thousand US dollars in the prior 2013 guidelines).

- **Competent Persons Report and Field Specific Report**: Prospective bidders are also asked to pay fifty thousand US dollars for a "Competent Persons Report" and twenty-five thousand US dollars for a "Field Specific Report".

- **Nigerian content**: Interested bidders are expected to demonstrate their commitment to developing local manpower and supporting indigenous service providers.

- **Farm-out process**: The Guidelines explain the key terms that are expected to be included in the farm-out agreement with the OML holder. If the parties are unable to reach agreement within 90 days, the DPR can be notified and will intervene to adjudicate the applicable terms.

- **Government back-in right**: The Government expressly reserves its right to take a participating interest in the marginal field. No further detail is provided and it is difficult to assess exactly what that right entails – necessitating a close examination of the back-in rights applicable to the relevant OML.
Considerations for participants

- **Title and bankability:** Marginal fields raise novel legal title considerations. This can be challenging for conventional lending structures and for investors.
    - The marginal field holder does not appear to possess a direct interest in the OML; instead it obtains a contractual interest by virtue of the farm-out agreement, which is akin to a sub-lease from the OML holders.

    - This raises questions about the validity of the marginal field interest where the OML expires or is revoked and the position of the marginal field holder before the DPR and the Government.

    - The Guidelines partially address this issue by stating that the marginal field farmee has the same rights as an OML holder (including the right to deal directly with the DPR) and all rights, interests and obligations of the OML holder are transferred to the marginal field farmee through the farm-out agreement. However, this position has not been tested before the Nigerian courts and the precise legal effect of the Guidelines is unclear.

- **Farm-out process:** A winning bidder obtains the right to enter into a farm-out agreement with the owners of the wider OML, which allows it to explore, produce, and take any petroleum encountered in the marginal field area, in return for paying consideration and a royalty to the superior OML holders. While a relatively customary form of agreement has developed, there can be many contentious issues:
    - The marginal field holder will assume all liabilities in relation to the marginal field area, including environmental and decommissioning matters. This can raise payment security demands from OML holders to support this allocation.

    - The parameters of the farmed-out marginal field area may raise questions about how discoveries that either straddle or lie deeper than the field boundaries should be allocated.

    - Alongside the farm-out, it will be necessary for marginal field owners to secure adequate access to neighbouring infrastructure to ensure production can be exported from the field – often owned by the superior OML holder. This may be difficult to negotiate and there can often be complex issues around how losses from pipelines are to be shared amongst the various users.

- **Five years to develop or lose:** The Guidelines appear to set an effective five year term for the award of the marginal field, and require progress in the development of the field to be shown before then (failing which the farm-out agreement can be made "void" or not be renewed). The DPR has previously warned the owners of undeveloped marginal fields that if they do not proceed to develop the fields within a set period, they risk losing them. Earlier this year, the DPR revoked 11 marginal fields.

What's next?

The Guidelines reveal that the DPR's expectation is for the final stage of the process, signature of a farm-out agreement, to be reached within six months of the 1 June 2020 announcement. Whilst it is possible that prospective bidders could complete their evaluation of the fields, submit bids and negotiate and finalise a farm-out agreement within six months, progress could well be disrupted by the low oil price environment and the ongoing COVID-19 pandemic. The appetite of the superior OML holders to engage with this process and quickly conclude farm-out agreement terms will have a significant bearing on meeting this timetable.

While the current circumstances are challenging headwinds for any award process, marginal fields may be less susceptible to the impact of low oil prices as they tend to be smaller in scale, require less capital to develop and are near-term development opportunities.