

# MINISTRY OF PETROLEUM RESOURCES

## DEPARTMENT OF PETROLEUM RESOURCES

7, KOFO ABAYOMI STREET, V/ISLAND

FAH. No. 4611777  
Telephone: 27478  
Website: www.dprnigeria.com



Ref. No. PI.LD/880.T  
Date: 1<sup>st</sup> April, 2011

The Hon. Attorney-General of the Federation  
And Minister of Justice  
Federal Ministry of Justice  
Shehu Shagari Way  
Maitama, Abuja FCT  
Nigeria

*Handwritten notes:*  
SAs  
Examine the attached document and  
advise on the same  
Very truly yours,  
5/4/11

Dear Sir

**RE: RESOLUTION AGREEMENT BETWEEN FGN, SHELL NIGERIA  
ULTRA-DEEP, MALABU OIL AND GAS LIMITED, NNPC, NIGERIA AGIP  
EXPLORATION AND PRODUCTION COMPANY NIGERIA LIMITED  
(SNEPCO) IN RESPECT OF OPL 245-NNPC'S DIRECTIVES.**

The above subject and the Letter with Ref; No.; HA/GF/FMPR/2011/VOL.1/2 dated 9<sup>th</sup> February 2011 from the Office of the Honourable Attorney-General of the Federation and Minister of Justice requesting for our comments on the attached draft Block 245 Resolution Agreement refers, please.

2) In order for the issues to be fully appreciated, the Honourable Attorney General's indulgence is most respectfully craved to allow us present a brief background on the issues regarding OPL 245.

### OPL 245-BRIEF BACKGROUND

OPL 245 was allocated to Malabu Oil and Gas Company Limited (an indigenous company) in April 1998 on a Sole Risk basis. OPL 245 is located in water depths above 1,000m in Nigeria's territorial waters off the Coast of the Niger Delta. Malabu and Shell Nigeria Ultra Deep Limited (SNUD) a special purpose vehicle of Shell Petroleum Development Company Nigeria

Limited (SPDC) concluded arrangements under which SNUD farmed into OPL 245 by way of a transfer of a 40% undivided interest in OPL 245 from Malabu to SNUD subject to final approval of the Deed of Assignment by the Federal Government of Nigeria. However, before the approval of the Deed of Assignment could be given by the Federal Government, the Government on the 2<sup>nd</sup> of July 2001 by way of a revocation withdrew the allocation of OPL 245 from Malabu Oil and Gas Company Limited.

In May 2002, following a bidding process involving SPDC and Exxon-Mobil, SPDC was awarded Contractor Rights in OPL 245 and in December 2003 executed a PSC with the NNPC, lease holders to OPL 245. Following a judicial challenge of the revocation of its licence by Malabu Oil and Gas Limited at the Supreme Court, a settlement judgment was entered into by Malabu Oil and Gas Limited and the Federal Government which resulted in Government re-awarding OPL 245 to Malabu Oil and Gas Limited in 2006 thereby vitiating the PSC between NNPC and SPDC in respect of the OPL.

Subsequent to the re-allocation of OPL 245 to Malabu Oil and Gas Limited, SPDC through SNUD brought arbitration under the Netherlands-Nigeria Bilateral Investment Treaty (BIT) against the Federal Government seeking the following Reliefs:

1. A declaration that the FRN has breached the Netherlands-Nigeria BIT;
2. A declaration that each such breach has caused harm to SNUD;
3. An award of such relief as the Tribunal determines, including, but not limited to, a declaration confirming that NNPC is the valid licence holder of OPL 245 and an order instructing FRN to procure NNPC to act in such a way as allows SNUD to implement the terms of the PSC in full restitution of its rights or, alternatively, monetary compensation in respect of the harm caused to the Claimant by the aforesaid breaches;
4. An award of the Claimant's costs for the arbitration;
5. An award of compound interest at a commercial rate on any monetary compensation from the date of the breach or the date payment should have been made or the date of award up to the date of payment;
6. Such other relief as the Tribunal determines appropriate.

Since the institution of the arbitral proceedings at the International Centre for the Settlement of International Disputes ("ICSID"-ICSID Case No.; ARB/07/18), the Parties (SNUD and FGN) have diligently pursued the arbitration to a point where the decision of the tribunal is now being awaited.

4. The fore-going represents the issues in respect of OPL 245 before the latest proposed Resolution Agreement which we shall now proceed to comment on.

5. In the proposed Resolution Agreement, 6 (six) entities, i.e. Federal Government of Nigeria (FGN), Shell Nigeria Ultra-Deep Limited (SNUD), Malabu Oil and Gas Limited (Malabu), Nigerian National Petroleum Corporation (NNPC), Nigerian Agip Exploration Limited (NAE) and Shell Nigeria Exploration and Production Company Nigeria Limited (SNEPCO) are the parties.

6. The Principal Terms of the proposed Resolution Agreement are as follows:

- (i) In consideration of an agreed sum to be paid by FGN to Malabu as determined in the Resolution Agreement (this sum is not stated in the draft), Malabu shall waive all and any interest or rights in Block 245 and grant its consent to the re-allocation of the interests in Block 245, by the FGN as agreed in the Resolution Agreement;
- (ii) SNUD agrees to the re-allocation of its interest in Block 245 to SNEPCO and SNEPCO will reimburse SNUD in respect of costs incurred under Clause 3 (of the Resolution Agreement) and costs of three hundred thirty five million and six hundred thousand US Dollars (\$335,600,000) incurred by SNUD related to the execution of the work-programme pursuant to the terms of the 2003 PSC and in consideration of this payment SNUD would consent to the re-allocation of the interests in Block 245, by the FGN as agreed in Clause 1.6 of the Resolution Agreement (i.e. re-allocation to SNEPCO).
- (iii) The FGN in exercise of its powers under the Petroleum Act Cap P10 LFN 2004 would re-allocate the interests in Block 245 jointly to NAE and SNEPCO and would commit that no Oil Prospecting License (OPL) shall be issued in respect of Block 245 other than to SNEPCO and NAE in accordance with the terms of the Resolution Agreement.
- (iv) Following the re-allocation to NAE and SNEPCO, SNUD shall on behalf of SNEPCO and NAE pay to the FGN a Signature Bonus as determined in the Resolution Agreement while the FGN shall

immediate; after deliver to NAE and SNEPCO an OPL in their joint names.

- (v) The issuance of the fresh OPL in the names of NAE and SNEPCO shall terminate the 2003 PSC between NNPC and SNUD and both NNPC and SNUD releases and discharges each other fully and effectively from all and any existing and continuing obligations that would otherwise survive the termination of the 2003 PSC except that this release shall not be deemed to extend to any claim or obligations related thereto and arising from this Resolution Agreement
- (vi) The fresh OPL shall be for a period of 10 (ten) years from the effective date and any subsequent OMLs derived there from shall be for an initial period of 20 (twenty) years.
- (vii) The sum of two hundred and seven million nine hundred sixty thousand US Dollars (\$207,960,000.00) in the escrow account under the Escrow Agreement dated 22<sup>ND</sup> December 2003 shall, following the termination of the Escrow Agreement by SNUD and FGN be paid to the FGN as Signature Bonus for the re-allocation of OPL 245 to SNEPCO and NAE.
- (viii) NAE shall upon the re-allocation of OPL 245 to NAE and SNEPCO deposit an agreed sum in an Escrow account to be jointly opened in the names of FGN and MALABU, this amount representing additional bonus due to FGN.
- (ix) FGN shall in turn release the sum in the joint escrow account to Malabu.
- (x) NAE and SNEPCO shall execute a Production Sharing Agreement (PSA) for the operation of OPL 245.
- (xi) The PSA shall be a Production Sharing Contract PSC as defined in section 17 of the Deep Offshore and Inland Basin Production Sharing Contracts Act, Cap D3, LFN 2004.
- (xii) The applicable fiscal terms applicable to any OMLs derivable from OPL 245 shall be the fiscal terms as provided in the Deep Offshore Act.

- (xiii) In the event that any change of laws or rules occurs that materially changes the applicable fiscal terms, the Parties to the Resolution Agreement shall agree to such modifications to the Resolution Agreement and or any agreements between them in furtherance thereof as will compensate for the adverse effect of such changes.
- (xiv) The Parties to the PSA (NAE and SNEPCO) being holders of OPL 245 following the re-allocation in accordance with the Deep Offshore Act shall be entitled to the allocation and lifting of Tax Oil under the PSA and shall remit the appropriate taxes to the relevant FGN agencies.
- (xv) The Signature Bonus to be received by FGN under the Resolution Agreement and the sum of \$335,600.00 incurred by SNUD related to the execution of the work programme pursuant to the 2003 PSC shall be treated as recoverable cost by NAE and SNEPCO in their operation of OPL 245.
- (xvi) The ISCID Arbitration between SNUD and FGN shall be withdrawn and all pending suits between the parties discontinued.
- (xvii) FGN shall grant full and unconditional exemption from any and all taxes, levies, duties, fees, and charges whatsoever (including by way of withholding) arising or relating to the re-allocation of interests (including payments between the parties) contemplated under this Resolution Agreement.
- (xviii) FGN including all its relevant agencies (NNPC) waives any right to acquire any participating interest in Block 245 and any OML derived there from (including, without limitation, any back-in-right which might be exercisable by NNPC) and waive any title to any portion of production from Block 245 other than the obligation of the Parties to pay royalty and taxes due from such production.

7. The preceding paragraphs represent the principal terms of the proposed Resolution Agreement. In our view, the terms of the Resolution Agreement as proposed are highly prejudicial to the interest of Government for the following reasons:

(i) Malabu is yet to pay the Signature bonus for the re-allocation of OPL 245 which is part of the Settlement Judgment in the suit between it and the Federal Government. Further more, FGN paying Malabu to relinquish its right in the Block, which right by reason of

the non-payment of the Signature Bonus is yet to mature would amount to paying Malabu for an asset it does not yet have.

Besides, it is completely contrary to the law and the Petroleum Act in particular for a party to consent to the allocation or re-allocation of an OPL or OML by the Minister.

(ii) SNUD has no interest in OPL 245 except the interest it has in the 2003 PSC between it and NNPC as the sole concessionaire to the Block. Even so, the interest in the 2003 PSC was terminated by the re-allocation of the Block to Malabu. Therefore, there is no basis either in law or fact for the assertion that SNUD has any existing interests in Block 245.

In deed, the main relief sought by SNUD in the ISCID arbitration is as follows: An award of such relief as the Tribunal determines, including, but not limited to, a declaration confirming that NNPC is the valid licence holder of OPL 245 and an order instructing FGN to procure NNPC to act in such a way as allows SNUD to implement the terms of the PSC in full restitution of its rights or, alternatively, monetary compensation in respect of the harm caused to the Claimant by the aforesaid breaches.

Therefore, it is preposterous to be asserting in the Resolution Agreement that SNUD has any interest in OPL 245 which the FGN by agreeing to pay money for would procure the consent of SNUD to re-allocate.

(iii) Granting OPL 245 to NAE and SNEPCO in the manner proposed in the Resolution Agreement would be contrary to the prevalent practice in Nigeria at the moment where Oil Prospecting Licenses are now granted on the basis of transparent and open competitive licensing rounds. FGN by committing to re-allocate the Licence to NAE and SNEPCO in this manner would be opening itself up to scandal and even future litigations more so when NAE hitherto the present Resolution Agreement was not a party to any of the transactions between the parties in respect of OPL 245.

(iv) Further more, the Resolution Agreement proposes to award OPL 245 to NAE and SNEPCO on a Sole Risk basis with out the FGN nor any of its agencies having a right of "back-in" in any future OML derived from the Block ( this is untenable because

parties can not by their Agreement exclude the operation of a Legislation in force).

FGN by agreeing to this proposal would be throwing away an enormous amount of financial resources more so when under the 2003 the NNPC was the concessionaire on the block. Indeed, there is no economic justification for removing NNPC as concessionaire and excluding the right of the FGN through NNPC to back-in or have a share of any production from the Block. Such an arrangement would leave for the FGN very little of the enormous potential economic value from the Block and create uncertainty in the interpretation and application of the relevant Nigerian Laws in this area.

In this regard, the FGN should not be unmindful of the still unresolved judicial cases involving the interpretation and application of the Deep Offshore Act and the Back-in-Right Regulations in the cases involving SAPETRO and the FGN on the one hand and Panfa and the NNPC on the other. By endorsing an Agreement such as is being proposed in this case, the FGN would be weakening its arguments in both cases and further throwing confusion in the practice of the law.

(xix) Further more, it is not sound policy for the FGN to be agreeing with private entities to under mine the intent and purpose of any future legislation or regulation it might make in respect of fiscal terms applicable to petroleum production operations. This is the direct effect of the term in the proposed Resolution Agreement requiring the parties to the Agreement to meet and agree to such modifications to the Resolution Agreement and or any Agreements between them in furtherance thereof as will compensate for the adverse effect of any future changes in the law.

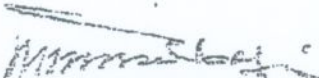
(xx) Also, the proposal in the Resolution Agreement purporting to give NAE and SNEPCO the right to lift Tax Oil under the PSA to be signed between the two upon the allocation of OPL 243 to both parties on the execution of the Resolution Agreement: would be contrary to the usual practice where the NNPC lifts Tax Oil on behalf of the FGN under the PSCs. It should be noted here that Tax Oil and its lifting confers several other economic advantages aside from the tax revenue payable to government.

- (xxi) Two of such advantages are the huge financial value arising from the arbitrage of the Tax Oil which would now go to NAE and SNEPCO and the enormous leverage that the FGN exercises by virtue of NNPC lifting the Tax Oil which would no longer be there where NAE and SNEPCO to lift the Tax Oil.
- (xxii) Also, the proposed Resolution Agreement provides for the treatment of the Signature Bonus received by the FGN under the Agreement and the sum of \$335,600.00 purportedly incurred by SNUD related to the execution of the work programme pursuant to the 2003 PSC as recoverable cost by NAE and SNEPCO. In effect, this means that the FGN would not have received any Signature Bonus on the Block and FGN would have indirectly paid for SNUD's claimed expenditure under the 2003 PSC.
- (xxiii) Further more, the matter of OPL 245 is already subject to arbitration at the instance of SNUD. That arbitral proceeding is far gone and a decision is expected any moment soon. After agreeing to submit to arbitration and expending so much time and expenses in the conduct of the arbitration, it would be counter-productive at this final stage to truncate what ever the outcome of the arbitration would be.
- (xxiv) The notion of a six party settlement at this stage is some thing that in our view would not be feasible. This is because Malabu is not a party to the arbitration. Therefore there is no basis for the Company to agree to a settlement at this stage, when there is no decision yet that is adverse to its interest in the block.
- (xxv) indeed, it is not in the best interest of the FGN at this stage to encourage any settlement of the issue outside the pending arbitral decision/award for the following reasons:
- (i) The position of the FGN has not been proven to be untenable or weak hence there is no real threat that the arbitral award would go against the interest of the Government; and
  - (ii) SNUD is seeking for either the Re-allocation of the Block to NNPC as Licensee and Shell as Contractor under the PSC between NNPC and SNUD; or in the alternative the award of the Monetary Value of the Block plus interest. In our view, none of these two



out-comes can leave the FGN without any viable options if any of them were to occur. Hence, the FGN is in an excellent position legally and economically at this time to hedge, pending the outcome of the arbitration and then choose what best option suits its interest after the result of the arbitration is known.

In conclusion, the Resolution Agreement as proposed is highly prejudicial to the interest of the Federal Government, more so when there is considerable leverage on the part of the FGN irrespective of the outcome of the arbitration. Government should therefore re-evaluate the proposal with a view to securing for the FGN a more advantageous out come from any resolution of the matter.



W.A. OBAFEHINWA

Director, Department of Petroleum Resources