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Legal Appraisal of the Nigerian Upstream Petroleum Unitization Regulations (NUPUR) 2023

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Abstract

Unitization is the process whereby parties come together in agreement to jointly develop a common reservoir that straddles across tracts, thereby minimizing production costs and creating efficiency generally. Unitization came into place to prevent the old system of capture, which encouraged competitive drilling, where parties were in a haste to capture more resources than the other, given that one party could tap from such oil from the adjoining reservoir of another party and divert it into their own reservoir and still own such diverted oil.This article has successfully discovered the loopholes which defunct regulations on unitization: The Petroleum (Drilling and Production) Regulation 1969, particularly at section 48 and The Guidelines for Unitization in Nigeria issued by the Department of Petroleum Resources 2008 (revised in 2019. These defunct regulations failed to provide important aspects of unitization namely; cross-border unitization, dispute mechanisms, allocation mechanisms, brown-brown fields, determination and redetermination, unit operators, relinquishment of interest by operators etc. which led to delayed unitization agreements. Due to these numerous loopholes, the Nigerian Upstream Petroleum Unitization Regulations (NUPUR) 2023 was enacted by the Nigerian Upstream Petroleum Regulatory Commission(NUPRC), the regulation provided for key issues that were not covered by the defunct regulation such as the notification of hydrocarbon reservoirs, cross-border unitization, determination of brown-brown fields, modification of unitization agreements, recognizance of straddling and non-straddling reservoirs, completion of PUA`s and UUOA`s and remuneration of consultants. However, even though the current enacted regulation tackled some issues, it failed to provide for the benchmark for determination and redetermination,created ambiguities, failed to provide a generalized system on how assets, interest and production costs will be shared among the license or lease holders, it was also silent on dispute mechanisms which may arise and finally it failed to give specific guidance on the complexities of multi-party agreements.This article investigates why Nigeria has few executed unitization agreements, which is a major challenge in the production of petroleum. It also makes a comparative analysis of unitization in Nigeria with other countries and suggested possible ways in which there can be more executed unitization agreements.

Keywords: Unitization, Petroleum Sector, Upstream, Regulation

1. Introduction

The "Rule of Capture" is a significant historical background which emerged in the early days of oil exploration in the United States (US), which led to the development of unitization in general.[1] It basically deals with "owning what you capture". Under this rule, a land owner is said to have possessory rights to oil produced in a common reservoir, as long as it is within the coverage of such owner`s land. The problem with this rule is that oil has the tendency to migrate due to its nature, therefore, there is probability that such oil will leave its reservoir and migrate to another adjoining land which share a common reservoir. When this happens, it leads to unhealthy competitive drilling between parties that have conflicting interest in a common reservoir.

This rule of capture was first applied in the case of *Brown v Spillman*,[2] the obiter dictum of the court was based on the fact that when a landowner carries out exploration activities and inadvertently extracts oil

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[1] C Kent, 'Surface and Subsurface Property Rights in Minerals: The Continuing Conflict' Journal of Private Enterprise (2019)34(2)<https://journal.apee.org/index.php/ajax/GDMgetFile/.2019_Journal_of_Private_Enterprise_V0l_34_No_2_Summer_PARTE3.pdf> accessed 10 July 2024.

[2] *Brown v Spillman* (1895) 155 U.S. 665

and gas from a neighboring property, causing the oil to flow into his oil well, he is entitled to ownership of such oil that was captured.[3] Therefore, Unitization was originated to prevent the shortcomings of the rule of capture.

However, in the 20th century, this rule received a lot of backlash and criticisms. One among many who criticized this rule is Doherty who alarmed the society that the rule of capture posed risk, one of which was competitive drilling. He then went further to state the harmful effects of competitive drilling. Therefore, states found a reason to enact conservation laws to combat the rule of capture. These laws were then enforced by the judiciary. However, it still applies in some places, Example, Texas. Modern arrangements were then made of unitization and joint development.

2. Meaning and Nature of Unitization in the Petroleum Sector

2.1 What is Unitization?

Unitization can be defined as a process that involves merging an oil and gas field managed by separate rights holders of the petroleum resources in separate tracts above a petroleum reservoir. It was created to reduce the impact of competitive drilling when a single petroleum reservoir spans two fields covered by different petroleum licenses or production sharing contracts held by different oil companies. This situation often leads to conflicts between the oil companies, so unitization was developed to address the conflicting interests of all parties involved while maximizing oil field recovery, which is a primary concern for the state.[4]

Unitization therefore allows the parties to come together to make an agreement, which is referred to as the Unitization and Unit Operating Agreement (UUOA), it governs the equity participation between both parties and the operational activities carried out in such straddling reservoir. Although, before the UUOA most parties enter into a pre-utilization agreement (PUA) due to the difficulties associated in creating the UUOA.

There are two common types of unitization stated below;

1. When parties willingly choose to unitize, it is called **voluntary unitization.**
2. It is called **compulsory unitization** when it is mandated by law or regulation or imposed in another way without the parties` consent. [5]

Unitization has various benefits, it prevents disagreements that could have arose between persons of conflicting interest, which could impede effective utilization.Most of these disagreements are as a result of competitive utilization of hydrocarbon found in the hydrocarbon reservoirs which straddles multiple licenses. Furthermore, Unitization allows for leveraging economies of scale and utilizing technical information, resources and facilities to maximum advantage. It also minimizes expenses and streamlines investments to efficiently develop straddling fields into a single unit.

In Nigeria, straddling field unitization is the most prevalent form, and it occurs when a reservoir extends across concession boundaries. On the other hand, non-straddling unitization involves combing concessions with separate reservoirs, while taking into account shared infrastructure or development benefits. Nevertheless, incorporating non-straddling reservoirs can lead to potential disputes.

Oil also migrates from one national boundary to another national boundary. For instance, a common reservoir exists between the exclusive economic zone of Nigeria and Sao Tome and Principe, where oil

[3] B Kramer, 'Unitization: A Partial Solution to the Issues Raised by Horizontal Well Development in Shale Plays' ALR (2015) 68 <https://law.uark.edu/alr/PDFs/68-2/68ArkLRev295-320Kramer.pdf> accessed 10 July 15 2024.

[4]R Chooramum, 'The Oil and Gas Industry`s Solution to One of Geology's Many Conundrums' (Lexocology, 2014) <http://documents.Lexocology.com/279fe7de-a081-4b57-84ea-8821421812f4.pdf> accessed 10 July 2024.

[5]R Olodude, 'An Appraisal on the Effect on Unitization of Oil Fields in Nigeria' Carnelian JL & Pol (2020) 1(83) <http://heinonline.org/hol-cgi-bin/get_pdf.cgi?handle=hein.journals/cjlp1&section=14''> accessed 10 July 2024.

straddles the borders of both countries. This led to the join treaty entered into by Nigeria and Sao Tome and Principe for development and unitization of petroleum and other resources found in their boundaries.[6]

3. The Old Regime and its Loopholes

The previous laws enacted for the unitization of oil fields in Nigeria includes the following;

a. Petroleum (Drilling and Production) Regulation 1969, particularly at regulation 48
b. The guidelines for unitization in Nigeria issued by the Department of Petroleum Resources 2008-revised in 2019.

One of the main reasons for the poor enforcement of unitization agreements in Nigeria was due to the lack of the defunct regulatory framework in providing precise policies for detailed unitization agreements. Due to the above reason it led to poor and delayed unitization contract agreements which are responsible for the loophole in Unitization in Nigeria. Therefore, a good regulatory framework will tackle these problems. In the old regime, unforeseen circumstances leading to a prolonged unitization agreement were not provided for in the regulations.

A close examination of the petroleum (drilling and production) regulation 1969 created room for ambiguity in relation to unitization, it states as follows;

> *The minister, after consultation with the licensee or lessee (referred to in this regulation as the "grantee") is satisfied that the relevant area or any part thereof forms part of a single geographical petroleum reservoir(referred to in this regulation as "the oil field") in respect of other parts of which any other license or lease is in force and that the field is susceptible of being developed as a unit in accordance with good oilfield practice…*[7]

From the above section the term "unitization" was not evenspelt out and properly enunciated, thereby creating room for ambiguities. Furthermore, the defunct regulation failed to provide concrete details for an appropriate delineation of reservoir boundaries which is necessary for utilization to be fair. Thus, such shortcoming might lead to conflicts as to license areas to be included and delayed unitization agreements. In addition to loopholes in the defunct regulation, these regulations failed to recognize both straddling and non-straddling reservoirs.[8]

In a unitization agreement, a unit operator is chosen by both parties to manage the common reservoir in terms of joint development and production. The old regime failed to provide specifications for the appointment of such operator, this led to companies appointing operators based on favoritism which led to one party having control over production decisions and benefitting from such decisions. This also created room for lack of expertise especially when such operator is selected based on favoritism. The involvement of an unqualified operator can result in suboptimal production methods, decreased recovery rates and ultimately reduced profits for all unit owners.

The defunct regulations did not provide detailed agreements that could tackle divestment concerns which led to unregulated relinquishment of interest by operators, ambiguous transfer of asset and liabilities, risk of asset stripping and abandonment, revenue and resources losses for the state and investors and inefficient resource management and development.

In the oil sector, oil fields consist of the green field, black fields and brown field. The brown field are fields that contain or likely to contain deposits of petroleum within it and other substances. A brown field may have been previously exploited and explored. The requirements forunitization of Brown –brown

[6]A Ni'ma, 'Role of Law in Exploration And Production Of Petroleum Resources' IBJ (2021) 1 <https://www.journals.ezenwaohaetorc.org/index.php/IBJ/article/view/1511> accessed 10 July 2024.
[7]Petroleum (Drilling and Production) Regulation 1969, s 48.
[8]A Egba and Others, 'Case Study of Unitization and Joint Development of Straddle Fields in Nigeria' (SPE Nigeria Annual International Conference and Exhibition, held at Lagos, August 2016) <https://onepetro.org/SPENAIC/proceedings-abstract/23NAIC/3-23NAIC/D031S013R005/525956> accessed 10 July 2023.

fields (where two or more parties are already into production) became a problem because there was no specific regulations and framework for unitizing brown fields.

The defunct legal frameworks also failed to provide dispute mechanisms for both parties in terms of disagreements that may arise. There could be disputes as to reservoir boundaries, license operators and interest; failure to provide for these issues is a major issue in unitization. Due to these many loopholes it has prolonged unitization agreements and many straddling fields have been found but there are fewer that have enforced Unitization and Unit Operating Agreement (UUOA). It is therefore a delay to the production of a large quota of oil thereby decreasing the capital income of nation.

The defunct regulations also failed to provide for cross-border unitization, where both parties can come into an agreement as to exploitation of their resources. It also failed to provide other factors to be considered in cross-border unitization.

Due to the delayed unitization agreements and its loopholes the Nigerian Upstream Petroleum Regulatory Commission introduced the Nigerian Upstream Petroleum Unitization Regulations (NUPUR) 2023, which is critically examined below.

4. Overview of the Regulation of the NUPUR 2023

The Petroleum Industry Act (PIA) 2021 authorized the Nigerian Upstream Petroleum Regulatory commission to make regulations in performing its statutory obligations under the Act.[9] One among these regulations to be deliberated on is the Nigerian Upstream Petroleum Unitization Act which was issued in the year 2023. The objective of the Act is to establish rules, principles and procedures for the implementation of unitization of unitization of oil and gas from a petroleum reservoir that extends beyond the boundaries of its licenses or lease area into an area to which another license or lease relates.[10]

This first key issue addressed is on preliminary activities to oil discovery, a licensee or lessee may in the course of conducting geophysical activities within their licensed or leased area, extend their data acquisition efforts up to 2 kilometers into adjacent license or lease areas, provided that such activities involve shooting across the boundary.[11] It further provides that the collection of geological data under these regulations requires the prior approval of the commission. [12]

All geophysical, geotechnical and geological data shall be interpreted and processed by the licensee or the lessee and made known by such licensee to the adjoining licensee or lessee. [13]As for mapping of traps, such licensee or lessee must identify and map all geological traps within their licensed or leased area that extend into adjacent license or lease areas and must do so in collaboration with and full disclosure of any affected parties.[14]

The second key issue addressed is notification of hydrocarbon discovery, when a licensee or lessee who discovers a petroleum reservoir in a geological trap within their licensed or leased area, which extends into an adjoining license or leases, must inform the commission of the finding within two weeks of suspending or abandoning the well.[15] The notification is followed by a full report within 60 days containing critical information.[16]

The third key issue addressed is the determination of the straddling reservoir, the regulation will therefore require a licensee or lessee to determine and confirm whether a reservoir that extends into their license or

[9] Petroleum Industry Act 2021 s 10(f).
[10]Nigerian Upstream Petroleum Unitization Regulation 2023, Regulation 1.
[11]Nigerian Upstream Petroleum Unitization Regulation 2023, Regulation 3(10).
[12]Ibid, Regulation 3(2).
[13]Ibid, Regulation 3(3).
[14]Ibid, Regulation 3(4).
[15]Ibid, Regulation 4(1).
[16]Ibid, Regulation 4(2).

lease area also straddles into adjoining licenses or leases.[17] If a licensee or lessee conducts exploratory activities, such as drilling a confirmatory well and the results indicate that the reservoir does not extend into an adjoining tract, the commission will officially declare the reservoir as non-straddling. When such reservoir straddles the commission will instruct the parties to enter into a unitization agreement.

If the licensee or lessee submits a rebuttal, the commission will review all the evidence presented by all the parties involved and make a final determination or whether the reservoir straddles or not, and its decision will be binding and conclusive.[18]

The fourth key issue addressed has to do with agreements, if the commission directs the joint development, the commission will then request that parties enter into a pre-unitization agreement (PUA) prior to the execution of a unitization agreement and execute a unitization agreement for the joint development of the reservoir.[19] When the straddling reservoir is a brown-brown field a unitization and unit operating agreement (UUOA) will therefore be executed by the parties.[20] These agreements must further receive approval from the commission before they can be formally executed and implemented by the parties involved.

The fifth key issue, if a petroleum reservoir extends beyond the boundaries of a license or lease into an adjacent unlicensed or unleased area and the licensee or lessee has declared a commercial discovery, the commission may either require the licensee or lessee to apply for a license or lease extension to cover the additional area, subject to meeting conditions set by the commission or conduct a bidding process for the unlicensed or unleased area that the reservoir extends into.[21]

The sixth key issue involves parties in a joint appraisal program under a pre-unitization agreement can declare a commercial discovery as per section 78(8) (a) of the Act.[22] Upon making this declaration, they can apply to the commission for approval to forego a unit agreement and instead submit separate field development plans. The commission will approve this declaration and separate development application within 90 days if it determines that doing so will not lead to reduced overall maximum economic recovery, increased overall capital and operating costs and lower overall royalty revenues from the commercial discovery.[23]

The sixth issue spelt out the issues to which parties to a pre-unitization agreement (PUA) shall have at least 12 months to finalize and execute the PUA from the date the commission mandates joint development of the reservoir as a unit. Similarly, the parties to a unitization agreement shall have a minimum of 12 months to conclude and execute the unitization and unit operating agreement from the date the commission gives its direction. [24]

The seventh key issue explains that if any one or more parties to a pre-unitization agreement are already producing petroleum independently from their respective areas before the decision to unitize the reservoir, they may continue producing until the pre-unitization agreement is executed. However, the commission reserves the rights to order the termination of these operations if it believes they may hinder optimal petroleum recovery or infringe on the rights of other licensees or lessees.[25]

Another important key issue addressed is the appointment of an independent consultant. A consultant in a unitization agreement is an independent expert who guides and provides specialized services to parties

[17]Ibid, Regulation 5(1).
[18]Ibid, Regulation 5(5).
[19]Ibid, Regulation 6(1).
[20]Nigerian Upstream Petroleum Unitization Regulation 2023, Regulation 6(2).
[21]Ibid, Regulations 7.
[22]Ibid, Regulations 8(1).
[23]Ibid, Regulations 8(3).
[24]Ibid, Regulations (9).
[25]Ibid, Regulations (10)

involved in the agreement. When the licensees or lessees are unable to agree on the terms of a unit agreement within the specified timeframe, the commission may issue a written directive requiring them to jointly appoint an independent consultant to develop the agreement`s terms and conditions.[26] The commission will determine the terms and conditions of the consultant`s appointment. If the licensees or lessees fail to appoint a consultant within 90 days of the commission`s directive, the commission will appoint one on their behalf.

The parties will be responsible for the paying the consultant appointed, if the parties cannot agree on the consultant`s remuneration, the commission will determine the amount. Failure to pay the consultant`s remuneration will considered a breach these regulation, and the defaulting party will be required to pay the amount due, plus an administrative fine equal to 100% of the remuneration, in addition to the original amount owed to the consultant. [27]

Determination and redetermination are needed in a unitization. Unitization is the initial assessment of the parties` interests and rights in the reservoir or field conducted when the unitization agreement is first implemented. This initial determination established the parties` ownership percentages, production sharing and other key terms. Redetermination on the other hand is an adjustment and analysis of the parties` interests and rights initiate in response to significant reservoir or field changes, such as new discoveries or revised estimates.

Parties to unit agreement may modify the agreement, subject to the approval of the Commission. When both parties have not provided a date for determination and redetermination, the date of completion of such determination and redetermination will be assumed to be the effective date.[28]

The final key issue addressed is accounts for cross-border reservoirs, which has to do with how to handle situations where the reservoir extends into international waters or another country`s territory. A good scenario is the Gulf of Guinea straddling oil reservoirs. Sao Tome and Nigeria has overlapping exclusive economic zone, which the United Nation Convention on the Law of the Sea, encourage parties to come together and jointly exploit their resources.

Unitization of straddling reservoirs like the examples given above that extend beyond Nigeria`s borders will be executed in accordance with relevant international treaties or agreements that Nigeria has ratified. If no such treaties or agreement exist, unitization will be based on consultations with the relevant authorities of the adjacent jurisdiction[29].

4.1 Criticisms of the NUPUR 2023

a. Date on finalizing pre-unitization agreements and unitization agreements

Section 80(3) of the Petroleum Industry Act 2021 provides as follows:

> *The commission may, upon receipt of a notification under subsection (1) direct the applicable licensee or lessee to enter into a unit agreement to develop the petroleum reservoir as a unit, within a period of time to be determined by the commission, which shall not be less than 2 years."*

This section is contradicting the provisions of regulation 9 of the NUPUR 2023, whether both Pre-unitization agreement and unitization agreement have a minimum of 12 months and not two (2) years to develop their reservoirs and finalize their agreements. This has created ambiguities as to the date of

[26]Nigerian Upstream Petroleum Unitization Regulation 2023, Regulations (11).
[27]Ibid, Regulations 11(6).
[28]Ibid, Regulations (13).
[29]Ibid, Regulations 14(1).

completion; however, even though the PIA would preside over all other subsidiary regulations from it, it still creates a room for doubts.[30]

b. Determination and Redetermination

There is no provision of the benchmark for determination and redetermination clauses in the NUPUR 2023.The regulation only made provisions on the date for determination and redetermination. Both determination and redetermination are complex features of a unitization agreement and therefore has to be given more focus.

c. Allocation Mechanism

The regulation failed to provide a guide on how production costs, reimbursement procedures and benefits would be shared among license holders. This means that the interest of both parties could lead to disagreements which bring about delayed unitization agreements

d. Dispute Resolution

When parties may have conflicts as regards unit operators, consultants, allocation of interests etc, there is no provision in the regulation as to how these conflicts may be resolved among the parties. It will be better if the regulation could therefore tackle unforeseen circumstances

e. Multi-party Agreements

The guidelines did not specifically cover complexities in agreements involving multiple parties, having multiple licenses over an oil reservoir.

5. Comparison with Other Countries

Brazil

The national petroleum agency in Brazil has a duty in regulating and overseeing unitization agreements. Brazil laws precisely the Pre-salt law requires the ANP (National Petroleum Agency) to approve unitization agreements, if parties to a common reservoir have delayed their agreements and refuses to sign a unitization agreement based on the ANP report will have the agreement ended and further production activities will not be carried out on the field.

The NUPRC`s direct involvement and participation in the process of unitization agreements is limited. There are not up to 10 successful unitization agreements in Nigeria, since the bodies for unitization have been ineffective in successfully enforcing the obligations of the parties and ensuring there are less delayed agreements.

United States of America

The USA government ensures the protection of correlative rights, the legal principle of correlative rights ensures that all landowners or mineral right holders in a shared reservoir or field have a proportional entitlement to extract resources, such as oil or gas, based on their individual ownership stakes. The principle guarantees a fair share of resources for each owner, preventing anyone owner from unfairly depleting the reservoir or field. By promoting efficient production, preventing waste and safe-guarding the owners` rights, correlative rights are essential when multiple owners have interest in the same reservoir or field, this principle is typically upheld through regulatory frameworks and court rulings.[31]

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[30]N Ole, ‘ Maximizing Economic Potentials And Eliminating competitive drilling through unitization agreements: An appraisal of the Nigerian upstream petroleum regulatory commission`s regulations 2023’ (Mondaq, 2023) <https://www.mondaq.com/nigeria/oil-gas--electricity/1355724/maximising-economic-potentials-and-eliminating-competitive-drilling-through-unitisation-agreements-an-appraisal-of-the-nigerian-upstream-petroleum-regulatory-commissions-regulations-2023> accessed 10 July 2024.

[31]J Weaver and D Asmus, ‘Unitizing Oil and Gas Fields Around the World : A Comparative Analysis of National Laws and Private Contracts’ Houston Journal of International Law 12 (2006) 28 (1) <https://www.researchgate.net/publication/228257352_Unitizing_Oil_and_Gas_Fields_Around_the_World_A-

There is no provision in the Nigerian regulation for fair shares of resources between the parties, this is however due to the fact that the Nigerian government has ownership of the mineral resources as opposed to the USA.

Another important comparison is that of the amount of unitization agreements enforced successfully. In comparing unitization agreements in Nigeria and the USA, the USA has more agreements executed in unitization than that of Nigeria with fewer unitization agreements.

6. Conclusion and Recommendations

The NUPUR 2023 has demonstrated a lack of foresight in neglecting to stipulate comprehensive provisions governing unitization agreements, thereby precluding the establishment of a paradigmatic structure for parties to emulate. This egregious omission has, in turn, engendered a proliferation of diverse agreements models crafted by parties, capitalizing on the flexibility and perpetuating profound ambiguities. The modification of the NUPUR 2023 in order to tackle unforeseen circumstances in a unitization agreement will lead to the effectiveness in executing unitization agreements.

There should be more detailed provisions on the benchmark of determination and redetermination, as these are key features of unitization agreements. It is imperative that the guidelines incorporate stipulations pertaining to dispute between license holders, a contingency which is inevitable in the context of unitization agreements. The guidelines ought to elucidate explicitly the participating interest and production cost of license holders involved, thereby clarifying the extent of their respective obligations. In respect of multi-party unitization agreements, the guidelines omitted the complexities that could be faced when there are multiple license holders, this is needed in order for the guidelines to sync with the reality of multi-party unitization agreements.

The contradiction of certain details as to the deadlines for the completion of pre-unitization and unitization agreements can be clarified by making the PIA 2021 to be in correspondence with the NUPUR 2023, this will reduce ambiguities in many unitization agreements. In imbibing the tradition of the ANP in Brazil, NUPRC should also be active in ensuring that there are less executed unitization agreements, by showing full involvement in unitization agreements.[32] The government should also be active in ensuring unitization agreements by the grant of incentives as a strategy to attract parties to unitization agreements in order to curb few executed unitization agreements.

Comparative_Analysis_of_National_Laws_and_Private_Contract/link/5526a17f0cf2f6e65169e0b7/download?_tp=eyJjb250ZXh0Ijp7InBhZ2UiOiJwdWJsaWNhdGlvbilslnByZXZpb3VzUGFnZSI6bnVsbH19> accessed 10 July 2024.

[32] Weaver and Asmus, (n 31).