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# Implementation Framework and Potential Implications of the Domestic Crude Supply Obligations ("DCSO")





Authority (“NMDPRA” or the “Authority”) are responsible for the implementation of the DCSOs. The Commission, however, has oversight responsibility for ensuring effective implementation.

This is notwithstanding the Minister of Petroleum’s right of pre-emption of petroleum and petroleum products in the event of a national emergency under the First Schedule of the PIA.<sup>2</sup>

The focal role of the Authority as it pertains to DCSOs is providing the Commission with the crude oil requirements for operational refineries and notifying the Commission of

## INTRODUCTION

While reiterating commitment to the development of the domestic crude oil market driven by willing buyer-willing seller arrangements, the Petroleum Industry Act 2021 (“PIA”)<sup>1</sup> permits the imposition of Domestic Crude Oil Supply Obligations (“DCSO”) by the Nigerian Upstream Petroleum Regulatory Commission (“NUPRC” or the “Commission”) on lessees of upstream petroleum operations (“lessees”) towards enhancing local refining capacity, preventing shortages and inadequate supply, supporting strategic economic development and promoting energy security.

## ROLES OF REGULATORS

Both the Commission and the Nigerian Midstream and Downstream Petroleum Regulatory

any shortages or inadequate supply conditions affecting local refineries on a regular basis.<sup>3</sup> any shortages or inadequate supply conditions affecting local refineries on a regular basis.<sup>3</sup>

On the other hand, the Commission's responsibilities with respect to DCSOs include allocating production quotas to lessees,<sup>4</sup> publishing the crude oil requirements of operational refineries as provided by the Authority<sup>5</sup> and designating refineries for the sale of crude oil under the DCSO arrangement.<sup>6</sup> To facilitate sales transactions between producers and local refiners, the Commission is mandated to publish crude requirements of operational refineries on its website and in 3 national newspapers for a period of six months on the 1<sup>st</sup> of January and 1<sup>st</sup> of July of each year.<sup>7</sup>

<sup>[1]</sup> Section 109 of the PIA

<sup>[2]</sup> Ibid, section 3(3).

<sup>[3]</sup> Section 109(3) of the PIA and Regulation 11 of the Production Curtailment and Domestic Crude Oil Supply Obligations Regulations 2023 (“PCDCOSOR”)

<sup>[4]</sup> Regulation 5 of the PCDCOSOR

<sup>[5]</sup> Regulation 10(1) of the PCDCOSOR

<sup>[6]</sup> Regulation 14 of the PCDCOSOR

<sup>[7]</sup> Regulation 10(2) of the PCDCOSOR



## KEY CONSIDERATIONS<sup>8</sup>

When identifying and selecting licensees and lessees for DCSO arrangements, the Commission will consider the proximity and accessibility of the supply location to the refiner, as well as whether the crude specifications match the domestic supply requirements. Where multiple licensees or lessees meet these criteria, the Commission will allocate DCSO volumes based on each producer's weighted proportion of its total production, taking into account existing refinery supply contracts, crude export contracts, Technical Allowable Rates<sup>8</sup>, and production quotas.

## IMPLEMENTATION

To ensure a steady supply of crude oil to the domestic market, the Production Curtailment and Domestic Crude Oil Supply Obligations Regulations 2023 (“PCDCOSOR”) prioritizes domestic supply obligations over exports commitments,<sup>10</sup> even where production in a quarter falls below allocated production quotas.<sup>11</sup> In reinforcing this priority, Regulation 9(2) of the Production Curtailment and Domestic Crude Oil Supply Obligations Regulations 2023 (“PCDCOSOR”) gives the Commission the authority to curtail crude oil exports by processing and approving export

permit applications, ensuring that export volumes do not interfere with DCSOs imposed on lessees.

On the commerciality of the imposition of DCSOs on lessees, Section 109(4) of the PIA provides that the terms of crude oil supply under the DCSO shall be negotiated between the producer and the refiner based on current international market prices.<sup>12</sup> Additionally, local refiners are required to provide payment guarantees as requested by the producer and to make payments either in Naira or US Dollars, as agreed upon by both parties.<sup>13</sup>

As part of its administrative oversight, the Commission is responsible for ensuring the dissemination, publication, and notification of refiners with information regarding the volume and quality of crude allocated, producers with DCSOs, potential offtake locations, and the terms and conditions of sale, including pricing, currency of payment, and payment guarantees.<sup>14</sup>

To ensure monitoring and compliance, Regulation 16 of the PCDCOSOR requires lessees to submit monthly reports on production performance based on allocated quotas and the utilization of production for DCSO and export to the Commission.

<sup>[8]</sup> Regulation 13 of the PCDCOSOR

<sup>[9]</sup> Technical Allowable Rates (TAR) refer to the assigned daily subsurface withdrawal limit of petroleum, which may be minimum or maximum permissible rate or both.

<sup>[10]</sup> Regulation 9 of the PCDCOSOR

<sup>[11]</sup> Regulation 15 of the PCDCOSOR

<sup>[12]</sup> Regulation 10(5) of the PCDCOSOR

<sup>[13]</sup> Section 109 (4)(c) of the PIA, Regulation 14(2)(3) of the PCDCOSOR, Paragraph 4.1 of the Guidelines for the Operationalisation of Domestic Crude Oil Supply Obligations (the “Guidelines”)

<sup>[14]</sup> Regulation of the PCDCOSOR, Paragraph 4 of the Guidelines

## SHORTAGES

Where the Commission receives a notification from the Authority about a shortage or inadequate supply of crude to operational refineries, it will request a written confirmation from the Authority detailing the volume of the shortage, the affected refineries, the crude specification or grade, the cause of the shortage, and any other relevant information.<sup>15</sup> Upon receiving this confirmation, the Commission will issue a Request for Quotations (“RFQ”) to all producers, requiring them to submit a quotation for the supply of the required volume to address the shortage.<sup>16</sup>

**Before issuing the RFQ, the Commission will ensure that each producer capable of meeting the refiners' crude requirement has allocated a portion of its forecasted production for domestic consumption to prevent supply shortages.<sup>17</sup>**

The RFQ shall include the required crude volume, supply location, crude specification, price, and timeline for submission. After receiving the response, the Commission will share this information with the affected refineries to facilitate contract execution on a willing buyer, willing seller basis.<sup>18</sup> If no contract is secured the contracted quantities are insufficient, or unreasonable demands are being made by the producer, the Commission will impose an obligation on the producer to supply the required volumes, which the producer must comply with.<sup>19</sup> Lessees whose productions are impacted by Force Majeure are also required to respond to the RFQ with an official Force Majeure declaration attached.<sup>20</sup>

Where a refinery is unable to independently secure future crude from the lessee or cannot obtain the minimum volume required for its forecasted period, it shall report the issue to the Commission, stating the specification of the crude required and the reason for its inability to secure crude.

Upon notification, the Commission shall intervene to prevent supply shortages by:<sup>21</sup>

- A** Directing a lessee to enter a crude purchase agreement with the refiner whereupon the refinery's request, the lessee has refused, failed, or neglected to do so.
- B** Where the shortfall is due to a stalemate over commercial terms other than price, the Commission shall request the negotiating parties to present the terms of their proposed contract. The Commission shall work to assist the parties reach an amicable agreement.
- C** Where the disagreement is over price, the Commission shall direct the parties to agree on a fair price using the Fiscal Oil Price differentials published by the Commission.



<sup>15</sup> Regulation 11 of the PCDCOSOR  
<sup>16</sup> Regulation 12 of the PCDCOSOR  
<sup>17</sup> Paragraph 2.10 of the Guidelines  
<sup>18</sup> Regulation 12(2) and (3) of the PCDCOSOR  
<sup>19</sup> Regulation 12(4) of the PCDCOSOR  
<sup>20</sup> Paragraph 5.1.2 of the Guidelines  
<sup>21</sup> Paragraph 2.17 of the Guidelines

## NON-COMPLIANCE

In addition to penalties as may be stipulated under the Supply and Purchase Agreement (“SPA”) between the refiner and lessee, the PCDCOSOR and the Guidelines for the Operationalization of Domestic Crude Oil Supply Obligations (the “Guidelines”) prescribe penalties for non-compliance and various infractions by parties. Some of these penalties are outlined in the table below:

INFRACTION	PENALTY
Failure to respond to the Commission’s RFQ or responding out of time <sup>22</sup>	Administrative fine of USD\$10,000 <sup>23</sup>
Failure to enter a contract for delivery of DCSO volumes pursuant to Paragraph 2.20 of the Guidelines <sup>24</sup>	Administrative penalty of 15% of the fiscal price of the DCSO imposed.
Failure to deliver volumes under a supply contract entered further to DCSO. <sup>25</sup>	Administrative penalty of 15% of the fiscal price of the DCSO imposed. <sup>26</sup>
Default in payment by the refiner	Suspension of DCSO allocation to the refiner for a period determined by the Commission <sup>27</sup>
Failure to offtake crude (pipeline, barging, or trucking deliveries)	Take or pay conditions shall apply <sup>28</sup>
Failure to offtake crude (marine deliveries)	Lessee shall sell the crude as a distressed cargo and the defaulting refiner shall be liable for liquidated damages under the SPA <sup>29</sup>
Failure to supply crude resulting in shortage to the refinery	Administrative penalty of 15% of the fiscal price of the DCSO imposed <sup>30</sup>

With respect to failure to deliver volumes for DCSO and default in payment by the refiner, penalties highlighted above shall be imposed after the Commission has issued a notice of default and entertained representations from the defaulting party (where provided) according to **Section 231 of the PIA**. All fines prescribed as penalties are required to be paid to the Commission.



<sup>[19]</sup> Regulation 12(4) of the PCDCOSOR

<sup>[20]</sup> Paragraph 5.1.2 of the Guidelines

<sup>[21]</sup> Paragraph 2.17 of the Guidelines

<sup>[22]</sup> Paragraph 5.1.1 of the Guidelines

<sup>[23]</sup> Regulation 18(1) of the PCDCOSOR

<sup>[24]</sup> Paragraph 5.2.1(a) of the Guidelines

<sup>[25]</sup> Paragraph 5.2.1(b) of the Guidelines

<sup>[26]</sup> The penalty shall not apply where failure is as a result of (i) Force Majeure, (ii) default of the refiner or (iii) any other reason acceptable to the Commission

<sup>[27]</sup> Paragraph 5.3.1 of the Guidelines

<sup>[28]</sup> Paragraph 5.5.1(a) of the Guidelines, the penalty shall not apply in instances of Force Majeure as defined in the SPA

<sup>[29]</sup> Paragraph 5.5.1(b) of the Guidelines, the penalty shall not apply in instances of Force Majeure as defined in the SPA

<sup>[30]</sup> Paragraph 5.6.1 of the Guidelines, the penalty shall not apply in instances of Force Majeure as defined in the SPA



## LEGAL AND COMMERCIAL IMPLICATIONS OF THE IMPLEMENTATION OF THE DCSOs

The prioritization of DCSOs over export commitments holds significant legal implications for producers as they may be mandated to divert crude intended for export to meet DCSOs. As highlighted earlier, the law requires the Commission to consider existing contracts while imposing DCSOs and in doing so, the Commission is to develop metrics that allow a portion of the forecasted production to be dedicated to domestic consumption by lessees on a non-discriminatory basis. This could potentially occasion material default in off-take agreements and existing financing commitments if not managed carefully by the Commission. Producers and project sponsors would also need to factor this new regime into their project planning and financing structures.

From a commercial perspective, the imposition of DCSOs could impact the voluntary nature of supply agreements which ought to be based on willing buyer-willing seller principles. While producers are still permitted to export crude, they are required to prioritize supply to local refiners as directed by the Commission. Although Section 109 of the PIA mandates that supply prices be negotiated based on consideration of international rates, this does not guarantee that producers will achieve the same level of returns as they would in the international market.

## INCORPORATING ROBUST FORCE MAJEURE CLAUSES IN PETROLEUM CONTRACTS

To safeguard against potential liabilities arising from the DCSOs under the PIA and PCDCOSOR 2023, it is crucial for producers to include comprehensive, water-tight Force Majeure clauses in their offtake contracts. These clauses should explicitly account for changes in government policies or regulatory actions, such as the imposition of DCSOs, which may impact their ability to fulfil export commitments. By doing so, producers can mitigate the risk of default or disputes and renegotiate contractual terms when domestic supply obligations take precedence over international off-take agreements.

## IMPACT OF DCSO ON LESSEES AND LICENSEES WHO CONTRACTED UNDER THE PETROLEUM ACT

# 01



### IMPACT OF DCSO ON LESSEES AND LICENSEES STILL OPERATING UNDER THE PETROLEUM ACT REGIME

**Section 311(9) of the PIA** expressly saves the Petroleum Act, allowing existing licenses and leases to remain in force until they expire or are voluntarily converted under the PIA. Except for the fiscal provisions of the PIA which are the base terms applicable, licences and leases granted under the Petroleum Act will continue to be governed by the provisions of the Petroleum Act until their termination, expiration or voluntary conversion<sup>31</sup>. Accordingly, for producers operating under the Petroleum Act, the PIA's DCSO regime would not apply to them.

### IS THERE A LEGAL FRAMEWORK FOR DCSO UNDER THE PETROLEUM ACT?

The Petroleum Act does not provide for a DCSO. However, a right of pre-emption is conferred on the Minister pursuant to section 7(1&2) of the Act, which provides that in the event of a state of national emergency, the Minister has the right of pre-emption over all petroleum and petroleum products obtained, marketed or otherwise dealt with under any licence or lease issued under the Act.

Accordingly, where the nation is faced with such an occurrence, paragraph 1(b) of the Second Schedule to the Act empowers the Minister to direct a licensee or lessee to supply petroleum products for the Federal Government, based on their refining capacity within Nigeria.



This includes delivering crude oil of specified quality and quantity to licensed refinery operators, provided the licensee or lessee possesses the required crude. Additionally, the Act obligates licensees and lessees to maximize, using existing facilities, their supply of petroleum or petroleum products to meet the Minister's demands. Failure of the licensee or lessee to comply with the Minister's requisition amounts to an offence punishable by conviction or fine.

Under section 305 of the Constitution of the Federal Republic of Nigeria (as amended) the declaration of a state of national emergency must follow certain procedural guidelines starting with the president issuing a proclamation via an instrument published in the official gazette of the Government of the Federation. It is noteworthy that a state of national emergency may only be declared under certain circumstances such as (i) when the Federation is at war; (ii) the Federation is in imminent danger of

<sup>[31]</sup> PIA 2021, Section 303(1) & (2).

invasion or involvement in a state of war; or (iii) there is any public danger which clearly constitutes a threat to the existence of the Federation. The Minister is also empowered to advise the President to declare a state of national emergency if public order and safety are jeopardized by insufficient availability of petroleum or petroleum products<sup>32</sup>.

Accordingly, under the Petroleum Act regime, the Minister's right of pre-emption is only exercisable in the event of war or a declaration of a state of national emergency by the president which is not a common occurrence, thus giving licensees and lessees more leeway to freely contract.

## 02



### IMPACT OF DCSO ON LESSEES AND LICENSEES WHO CONTRACTED UNDER THE PETROLEUM ACT

For the generality of licenses and leases governed by the provisions of the PIA either by termination or voluntary conversion, we believe that existing crude offtake contracts entered into by these licensees and lessees while operating under the Petroleum Act will not be retroactively governed by the PIA or the PCDCOSOR 2023. This serves as a legal safeguard, ensuring that the rights and obligations established under the Petroleum Act are preserved and respected, maintaining the status quo until the contract expires or is terminated. This safeguard is consistent with the legal principles surrounding retroactive laws as typified by the legal maxim: “**lex prospicit non respicit**” meaning “the law looks forward, not backward”. Accordingly, although constitutionally permitted (save in the case of criminal matters), unless clearly stated in the relevant statute, there is a general presumption against retrospective enactments. In the case of **Alewa v. Sokoto State INEC**<sup>33</sup>, the Court of Appeal Per Kekere-Ekun, J.C.A held, "Black's Law Dictionary (8th edition) defines a retroactive law as "a legislative act that looks backward or contemplates the past, affecting acts or facts that existed before the act came into effect.

A retroactive law is not unconstitutional unless



<sup>[32]</sup> Ibid, Section 7(5).

<sup>[33]</sup> (2007) LPELR-8388 (CA) (Pp. 20-21 paras. A). See also *Aremo II v. Adekanye* (2004) 13 NWLR (Pt. 891) 572.



In the case of *Lami Koro Ojokolobo & Ors V. Lapade Alamu & Anor*<sup>34</sup>, the Supreme Court Per Augustine Nnamani, J.S.C held, "It is a well settled principle of law that an Act of Parliament cannot be construed as having retrospective effect unless there are express words in the enactment showing such an intention. This is based on the presumption that the legislature does not intend what is unjust. Statutes are construed as operating only in cases or on facts which came into existence after the statutes were passed unless a retrospective effect is clearly intended. One of the more well known statements on this rule is that of Wright, J. in *Re Athlumney* (1898) 2 Q.B. 551 at 551,552 where he said- "Perhaps no rule of construction is more firmly established than this - that a retrospective operation is not to be given to a statute so as to impair an existing right of obligation, otherwise than as regards matter of procedure unless that effect cannot be avoided without doing violence to the language of the enactment. If the enactment is expressed in language which is fairly capable of either interpretation, it ought to be construed as prospective only" See also *Moon v. Durden* (1848) 2 Ex 22, 43. But the presumption against retroactivity is a presumption and is therefore not rigid and inflexible. Scarman, J. in *Carson v. Carson* (1964) 1 W.L.R. 511 at 517 said it is "one to be

applied always in the light of the language of the statute and the subject matter with which the statute is dealing." The presumption can also be overcome either by express words in the Act or by circumstances sufficiently strong to displace it.

An examination of the enabling statute<sup>35</sup> which grants the Commission the authority to make regulations on Domestic Crude Oil Supply Obligations (in this case, the Production Curtailment and Domestic Crude Oil Supply Obligations Regulations 2023), clearly reveals no intention for retrospective application to licensees and lessees who contracted under the Petroleum Act before their licenses or leases were terminated or voluntarily converted.

In our view, the presumption against retroactivity remains intact, and the current circumstances do not present sufficient grounds to override this presumption.

Consequently, crude offtake contracts entered into by licensees and lessees while governed by the Petroleum Act retain their legal validity until they expire or are terminated.



<sup>[34]</sup> (1987) LPELR-2392(SC) (Suit No: SC.42/1987)

<sup>[35]</sup> See section 109 of the PIA.

## CONCLUSION

The DCSOs introduced under the PIA represent a critical step toward enhancing Nigeria's domestic refining capacity and energy security. However, the successful implementation of these obligations will depend largely on the balancing act between regulatory oversight and the protection of existing contractual rights, project commerciality, bankability, amongst others. The Commission's role in curtailing exports to prioritize domestic supply demonstrates the government's commitment to supporting local refineries, but it also underscores the need for clear and fair regulatory frameworks that do not undermine existing contractual obligations or disrupt market dynamics. For producers operating under the Petroleum Act, although they have no domestic crude supply obligation, they must remain aware and mindful of the Minister's pre-emptive right to requisition crude for domestic use in the case of a declaration of national emergency or war by the President, which could still impact their operations. For producers currently operating under the PIA, the preservation of their contractual rights and obligations under crude offtake contracts and commitments entered during the Petroleum Act regime is a legal safeguard that protects them from retroactive application of the PIA's DCSO regime. However, they also must remain aware and mindful of the Minister's pre-emptive right to requisition crude for domestic use in the case of a declaration of national emergency or war by the President, which is also preserved under the PIA. As Nigeria gradually shifts to the PIA framework, producers must integrate robust risk management practices, such as effective Force Majeure clauses, creative financing structures,

etc., to mitigate any potential disruptions caused by changes in domestic supply obligations.

**Looking ahead, all industry stakeholders must engage in a forward-thinking approach that accounts for potential regulatory shifts while maintaining operational and commercial flexibility.**



It is important to note that the NUPRC has issued a Draft Amendment to the PCDCOSOR 2023 which was recently subjected to a Stakeholders Consultation held in accordance with Section 216 of the PIA. However, the draft amendments do not seek to alter the responsibility of a licensee or lessee to comply with supply obligations, but rather addresses issues related to administrative penalties, pricing, and circumstances under which the Commission may terminate a DCSO.



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