



ADDAX PETROLEUM CORPORATION

Memorandum

on the

Review of HB. 159, A Bill For An Act To Establish The Legal And Regulatory Framework, Institutions & Regulatory Authorities For The Nigerian Petroleum Industry, To Establish Guidelines For The Operations Of The Upstream And Downstream Sectors And For Purposes Connected With The Same (The Petroleum Industry Bill)

Delivered To

**The House of Representatives Joint Committee
on the Petroleum Industry Bill 2009**

July 30 2009

Honourable Chairman and Members of this esteemed Joint Committee,

We thank you for your kind invitation to present our views to the public hearings and contribute to the consultative process on the legislation currently under consideration by this Committee.

Introduction

Addax Petroleum is in support of many of the industry reforms originally contemplated by the Draft Petroleum Industry Bill, with the aim of encouraging both inward and domestic investment in the oil and gas industry and to ensure broad economic development and industrialisation of the nation.

Our principal concerns however relate to certain provisions of the Draft Bill particularly as currently contemplated by the OGIC's Inter Agency Team where recent drafts have contemplated the imposition of a particularly onerous fiscal regime which we believe will result in a significant fall in investment and eventually to a significant drop in Government Revenue through a lack of resource development.

Many of the concerns raised by the industry, as covered in the submission by the OPTS, as an umbrella organisation for the producing companies, are shared by Addax Petroleum although each company has particular concerns which may or may not be shared by others.

Addax Petroleum recognises that the development and implementation of legislation is the sovereign right of each and every nation and we greatly appreciate the opportunity given to offer our views and opinions upon the current Petroleum Industry Bill to the legislators in the Senate and the House of Representatives.

More than any other, the oil and gas industry today is a truly international business where the oil and gas operators are competing for exploration and production rights all over the world and where sovereign governments also have an opportunity to compete for investment by making their legal and fiscal framework attractive to investors.

The legislation currently being debated will have a long term impact on the development of the Federal Republic of Nigeria so it is of paramount importance that its ramifications are fully understood either through consultation with the oil and gas companies or by the engagement of third party advisors with experience in the sector.

Addax Petroleum in Nigeria

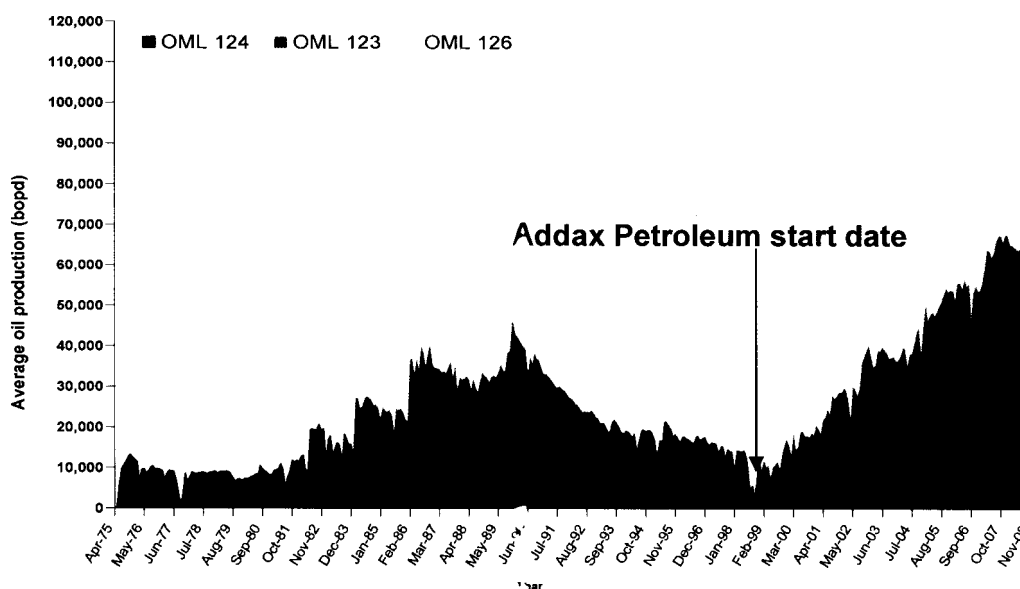
The history of Addax Petroleum in Nigeria offers an excellent insight into how oil and gas investment leads to increased Government take and rapid development of the indigenous natural resources and how future investment will be severely threatened by the passage of the Draft PIB as currently envisaged by the OGIC Inter Agency Team.

Addax Petroleum has operated in Nigeria since 1998 and remains one of Nigeria's outstanding success stories of recent years where during this period Addax has invested over USD 3 billion, paid taxes of over USD 5 billion, increased production from under 8,800 barrels per day to almost 110,000 barrels per day whilst at the same time significantly increasing reserves through an aggressive exploration programme. The Addax story is a good story for Nigeria, and Fiscal Stability has been, and continues to be, a critical part of this success story.

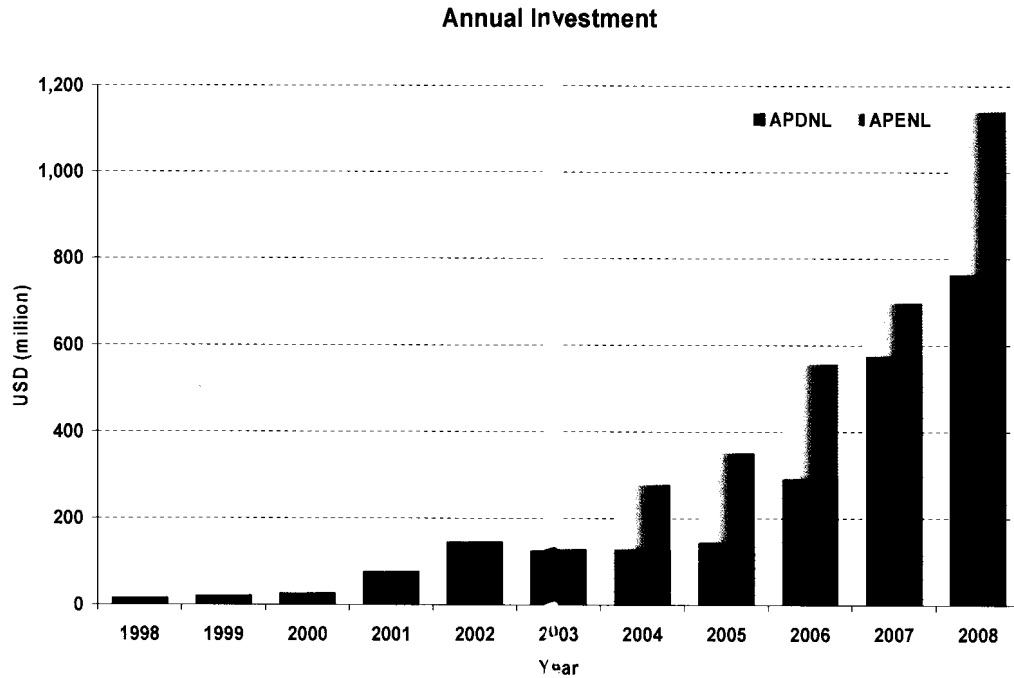
Addax's operations in Nigeria commenced with the acquisition of mature and under invested assets from Ashland which were the subject of two PSCs which now encompass OMLs 123/124/ and 126/137

The following graphs show a) the production rate from these properties from 1975 to 2008 in the period prior to and after the Addax acquisition and b) the investments made since 1998 and c) the consequent increase in Government Take

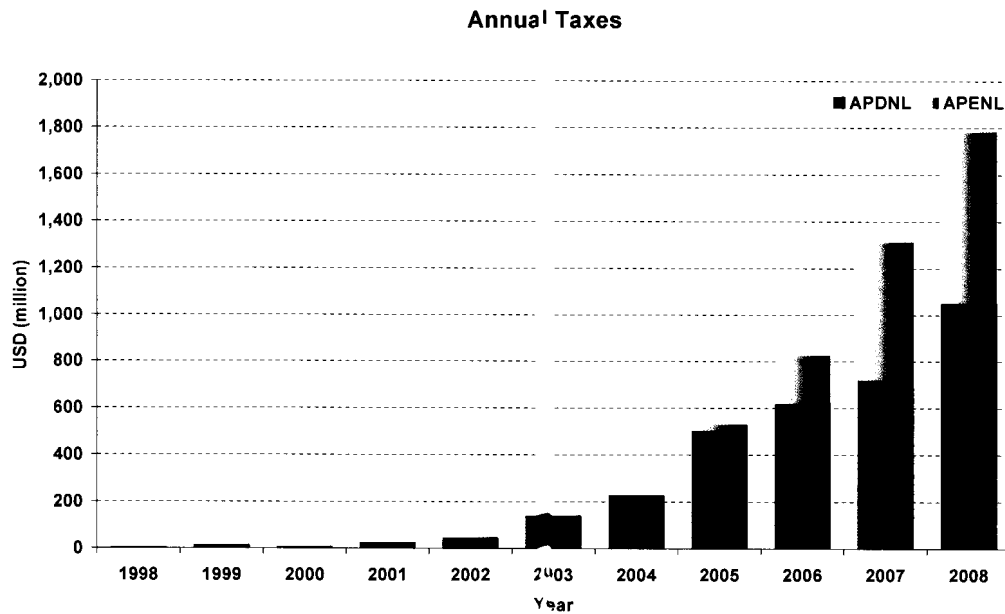
a) The following table shows the production growth from these assets since Addax took over as contractor in 1998 and the arrestment of a long term decline:



b) The following table shows the investments made since 1998 to 2008 totalling US 3,506 and in 2009 the Approved Budget is US1,007 Million:



c) The following table shows the total amount of PPT, Royalties and NNPC profit oil paid by Addax Petroleum subsidiaries from 1998 through to 2008, as set out in the various reports and filings made with FIRS, DPR and NNPC totalling US5,173 Million.



Making Nigeria an attractive destination for oil and gas investment will undoubtedly ensure an increasing Government Take for many years to come and create a great many employment opportunities for a growing population whereas the imposition of an onerous fiscal regime will have the opposite effect.

A Summary of Concerns in Regard to the Draft PIB

The concerns summarised below are those of the greatest significance to Addax Petroleum and which, if not addressed will result in lower investment in exploration and development of oil and gas resources in Nigeria.

We would be pleased to present each of these in detail to the House and Senate Committees at a time of your convenience.

a) Steep Increase in Tax and Royalty Rates

We have modelled our planned developments using the proposed fiscal regime in the Draft PIB and the proposals of the OGIC's Inter Agency Team and the increase in Government Take is so substantial to the point of making the projects uneconomic at current oil and gas prices

It cannot be the intent of the legislation to stop such developments proceeding.

The experience in other countries where there has been sudden and substantial increase in Government take has been for sharp reduction in foreign investment and long term falls in both production and taxes

Fiscal stability has been the foundation upon which we have invested in Nigeria over the past decade, which has resulted in the very significant increase in Government Take from the licence areas in which we operate, any legislative proposals which threaten this stability will inevitably delay and lower our investment profile .

b) Delays to Gas Developments

In all PSCs in Nigeria the rights of development relate only to oil, and in the case of gas discoveries a commercial development agreement must first be negotiated with NNPC

Each PSC is predicated on the right to participate in any gas project proposed, with the right to recover the costs and share in the profits, however to date no such commercial development agreement has been negotiated despite substantial gas reserves being discovered and the lack of such agreements severely hinder the development of domestic gas for power and industrial purposes as well as for export schemes.

The Draft PIB actually worsens the current situation in that it proposes a possible separation of oil and gas rights within the same contract area which is unnecessary and will be unworkable; the delays in gas development projects are as a result of a lack of a commercial framework under which they can be developed not an unwillingness to do so on behalf of the PSC Contractor.

Elsewhere in the world it is recognized that a licensee needs to hold exclusive rights to carry out exploration, and that there is no distinction between exploring for oil and exploring for gas as the result of the exploration activity could be either oil, or gas, or (most likely) both.

The development of gas resources in Nigeria today also requires fiscal incentives to be in place yet those currently in place are being withdrawn by the provisions of the Draft Bill and instead replaced with higher royalties and taxes. We have no doubt that should the Draft Bill be passed in its current form the implementation of the Gas MasterPlan will be seriously delayed

c) Breadth of the matters covered by the Draft PIB

It is unusual for a single piece of legislation to cover such a broad range of matters, and specifically for an Act to regulate an industry, to also include the fiscal rules applying to that industry.

In other Oil and Gas producing countries different Ministries are responsible for the regulatory issues as distinct from the fiscal issues (the Minister and Ministry of Petroleum Resources have authority to regulate the petroleum industry, while the Minister and Ministry of Finance have authority for fiscal matters). If Ministerial approvals or acts are required, which they are in many places, then different Ministers must be responsible.

Consequently the best approach is to separate this Bill into separate pieces of legislation, so that matters which are the proper responsibility of the Minister of Petroleum Resources are in one piece of legislation and matters which are within the responsibility of the Minister of Finance are in another.

This separation of fiscal provisions is important for many reasons, including the extensive provisions in other tax legislation regarding taxation administration. Investors in the petroleum sector need the certainty of knowing and understanding the full extent of the administrative rules which will apply to them.

The regulatory aspects of this bill are so extensive that it is appropriate simply to repeal the existing legislation in this area, but that isn't the case with the fiscal aspects. For fiscal matters it is more appropriate to specifically amend existing legislation, so that it is clear exactly what rules continue to apply.

d) Proposed Cap of 80% on Foreign Expenditure

The Draft PIB provides that only 80% of verified, benchmarked and approved expenditure incurred outside Nigeria will be deductible for the purposes of computing adjusted profit for taxation purposes.

Whilst the desire to support local industry is admirable, and supported by Addax Petroleum, if this provision was implemented it would have a significant adverse impact on Nigeria's revenues and at the same time make Nigeria a much less attractive place to invest.

The loss of tax deductibility for 20% of a project's capital cost is exceptionally onerous as a large proportion of capital expenditure on a project must still be spent abroad.

No operator will incur expenditure abroad if a truly equivalent product is available in Nigeria, the industry currently incurs expenditure abroad because there is no true equivalent available locally.

Forcing local procurement simply drives up costs on major capital items, which through both cost recovery and tax deductibility would lead to a significant lessening in government revenues.

Another problem concerning this provision is that it has retrospective effect. Many companies have made expenditure or ordered plant and equipment in good faith, in the expectation that it will be fully deductible over time, through depreciation. This provision would prevent them getting the deduction which they are entitled to today. It would be iniquitous to introduce any form of compulsion to source locally without a significant lead period and grandfathering past expenditure which is still being deducted.

e) Incorporation of PSC Company upon Commercial Discovery

The proposed requirement to incorporate a company to manage or operate the PSC on attainment of commerciality makes no rational sense to us as PSCs are predicated on the Contractor assuming all risks.

Its inclusion adds another level of risk for PSC Contractors particularly in regard to project funding for commercial development and its inclusion is inexplicable.

Conclusion

Addax Petroleum shares the deep concerns expressed by the OPTS and other Operators about the negative impact of both the PIB under consideration and the revisions to the PIB proposed in the Inter Agency Submission from the OGIC.

We strongly believe in Fiscal Stability to encourage new investment and generate increasing Government take however the attainment of the industrialisation goals set for Nigeria as a nation by President Yar'Adua will be very much harder to attain, in our view, should the PIB as currently drafted be passed into law.

We would humbly request the opportunity in the near future to present our concerns and solutions to the members of the House and Senate in greater detail and we thank you for your attention to our memorandum and for the opportunity given to present this document to this esteemed Joint Committee.