

# **LEVERAGING GAS FOR ECONOMIC GROWTH - THE EVOLVING NIGERIAN GAS SECTOR**

## **THE NIGERIAN TEMPLATE GAS SALE & AGGREGATION AGREEMENT (GSAA)**

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# Outline

- The Gas Sale And Aggregation Agreement
  - key terms and conditions
- Mitigating the risks: Credit security
- Implications for the banking and finance sector

# THE TEMPLATE GAS SALE AND AGGREGATION AGREEMENT

- Designed to present common terms for wholesale Gas Supply in Nigeria - it's a template
- **Highlights**
  - Gas Purchase Order
  - Conditions Precedent to effectiveness of obligations
  - Take or pay
  - Nomination intricacies
  - Payment security
  - Gas specification
  - Transportation
  - Transitional based pricing scheme [Emergency Period - To market based pricing]
  - Termination
- Payment Security
- Collateral Contracts

# BACKGROUND

- **The National Domestic Gas Supply & Pricing Regulations**
  - Domestic Gas Supply Obligation
  - The Aggregator
  - The Gas Purchase Order
  - Penalties for failure to supply DSO

# THE ROLE OF THE AGGREGATOR

- Conduct Due Diligence on B
- Issue a Gas Purchase Order to B
- Coordinate S & B
- Arrange for alternative purchasers of Gas
- Manage the escrow arrangements
- Relate with Government regarding Domgas supply

# THE GAS SUPPLY TRANSACTION

- Buyer approaches Seller further to a Gas Purchase Order issued by the GACN
- Buyer and Seller negotiate a Gas Sale & Aggregation Agreement (GSAA)
- GACN approves the GSAA and signs as 3<sup>rd</sup> Party
- Buyer negotiates and executes a Gas Transmission Agreement with NGC
- Escrow Agent executes an **Escrow Agreement** with Aggregator re: proceeds of gas sale transaction
- Typical gas sale transaction will run for **10 – 20 years**
- This structure will apply to all wholesale gas supply transactions in Nigeria until the gas market reaches maturity

# Conditions Precedent

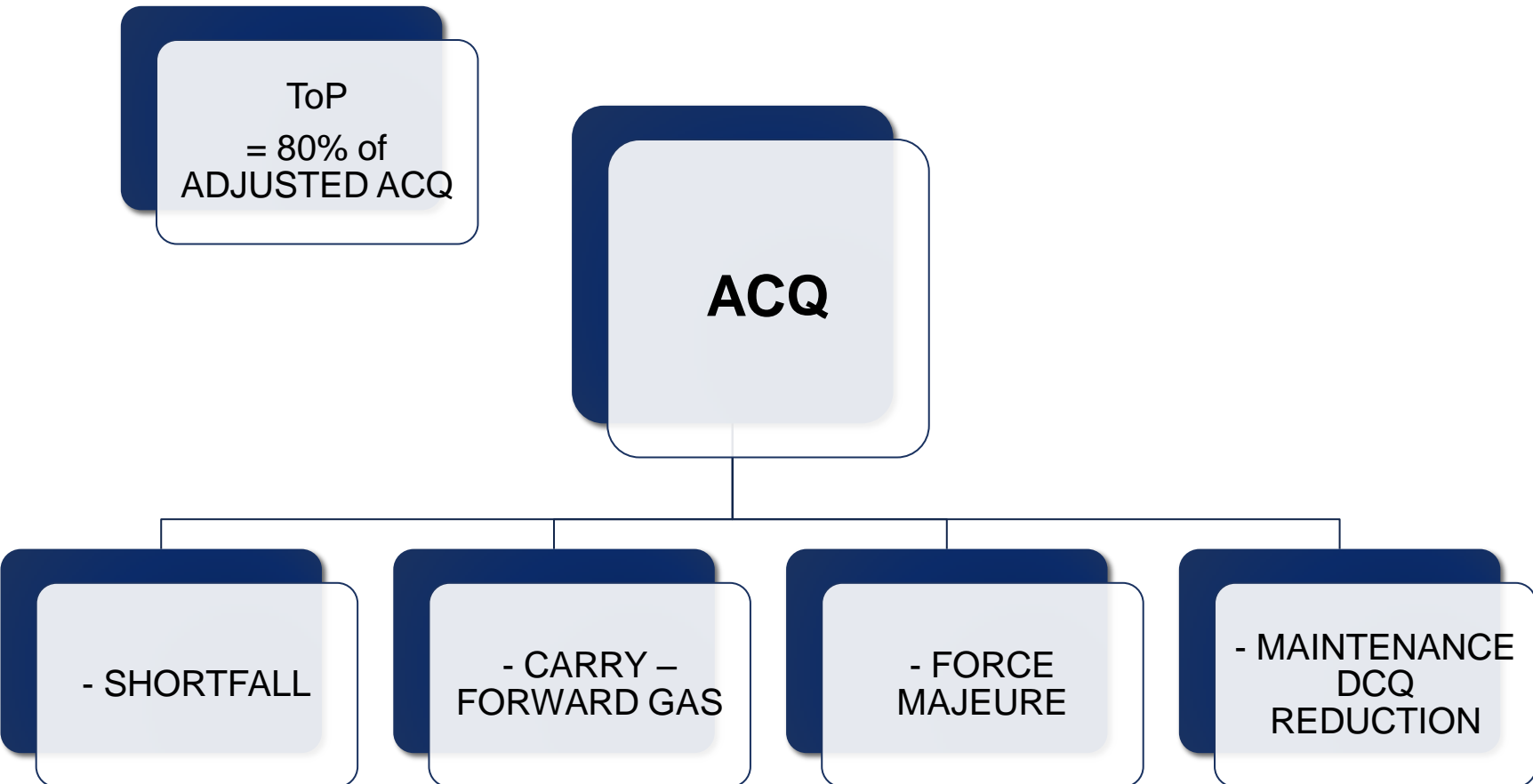
- Approvals for construction and operation of Seller & Buyer Facilities
- Execution of Construction Contracts
- Execution of Pipeline Use Agreement (where required)
- Execution of Tie-in Agreement (where required)
- Execution of Gas Transportation Agreement
- Allocation Agreement – required where there are more than one Seller at the Delivery Point
- Payment security/guarantees in place

# Nomination

- Buyer is required to provide a Good Faith Best Estimate of its hourly, weekly and monthly estimates of gas
- **Nominated Quantity** - Quantity of gas nominated by Buyer within a Nomination Period
- Daily Nomination - is a firm order/a confirmation and not an estimate
- Buyer & Seller will agree a range within which a nomination may vary from the previous day's Nomination
- Buyer may vary nomination within a limited time period



# TAKE OR PAY



# Take or Pay (ToP) Structure

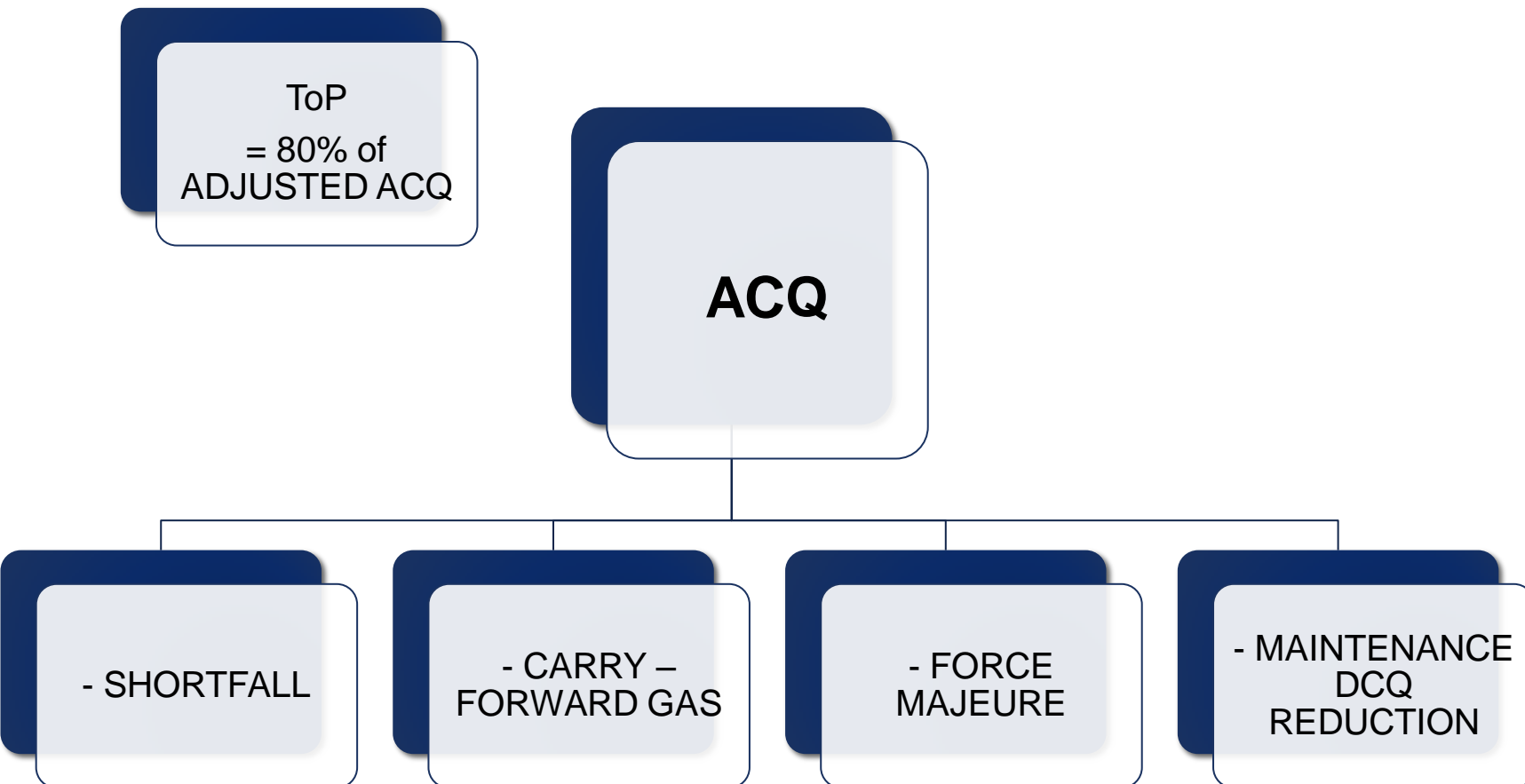
- The Commitment:

Buyer's obligation to pay for a quantity of gas delivered by Seller according to the contract.

Obligation to pay applies whether or not Buyer has taken delivery of the Gas

- Calculated on an annual basis. Reconciliations at the end of the year
- Annual ToP (**AToP**) amount is derived from the Annual Contract Quantity (**ACQ**) which is adjusted for: Maintenance (DCQ Reduction), Force Majeure, Shortfall & Carry Forward Gas
- **AToP**= 80% of Adjusted Annual Contract Quantity (**AACQ**)

# TAKE OR PAY



# Gas Specification

- Rule: Gas must conform to contract specification
- Buyer's remedies:
  - Right to reject Off Spec Gas with no liability
  - If rejected, Off Spec Quantity = Shortfall Gas
  - If accepted, payment for gas will be at a discount (90% of Contract Price)
  - Indemnification against any loss incurred for physical damage to Buyer's and Transporter's facilities, including cost of clearing and cleaning Buyer's and Transporter's facilities
  - Where knowingly taken, Seller is absolved of liability

# Shortfall Gas

- Applies where Seller supplies gas below nominated quantity
- Buyer's remedies for Shortfall:
  - cash compensation
  - right to procure alternative fuel and be reimbursed by Seller
  - redemption at a discount
- Ground for Termination where prolonged

# Annual Deficiency

- Annual Deficiency is ascertained at the end of each contract year.
- It occurs when the Buyer has:
  - not taken up to the ToP in a contract year
  - not paid for the volume of gas not taken
- Annual Invoice is issued and expected to be settled by Buyer within an agreed period of time
- Once settled, Buyer is eligible to recover the Outstanding Annual Deficiency (OAD) as **Make Up Gas**

# Make Up Gas (MUG)

- Results when an Outstanding Annual Deficiency (OAD) has been paid for
- **Note:** ToPQ has priority over MUG in any Contract Year
- MUG taken will reduce any OADs in the order in which they arose
- 2 year limit for MUG recovery
- MUG is recoverable at the prevailing price at time of recovery

# Carry Forward Gas (CFG)

- CFG is gas taken in excess of ACQ
- A percentage of CFG accruing in a Contract Year will adjust the ACQ for the following year



# Excess Gas (EG)

- Gas required by Buyer in excess of the **Maximum Daily Quantity**
- Seller's obligation limited – “Reasonable Endeavours” requirement only
- No obligation on Seller to deliver EG and therefore no Shortfall liability if it fails to deliver EG
- Excess Gas is sold at the Contract Price plus premium
- Excess Gas will reduce the ToP and ACQ

# Make Good Gas (MGG)

- Gas made available by Seller to Buyer in excess of nominated quantities
- An attempt by Seller to restore or “Make Good” Shortfall Gas and therefore reduce Shortfall liability
- To be taken by Buyer only on a “reasonable endeavours” basis
- Aggregator can help to find alternative Buyers for the MGG
- Sold at a discount on the Contract Price

# DELIVERY POINT, TITLE TO GAS, TRANSPORTATION

- The inlet flange of the nearest gas transmission pipeline to Seller's facilities [or as further illustrated in the schedule]
- Title to and risk in the gas to pass from S to B at the Delivery Point
- B to procure transportation from the Delivery Point at its own risk and expense

## 2. INVOICING AND PAYMENT

- Monthly invoices for Gas delivered  
[provided invoice for each delivery period is not less than pre-agreed daily minimum]
- Yearly reconciliations
- Payment by B into Escrow Account to be evidenced
- Payment to be made in Naira
- No set - offs allowed
- Disputed amounts to be paid into **Disputed Amount Account**

# DEFAULT IN PAYMENT

- Issuance of Notice of Non-Payment
  - To be issued **2 days** before payment due date
  - To give **5 days Grace Period** commencing the day after payment due date
- Buyer's failure to pay within the Grace Period will entitle Seller to trigger the payment security

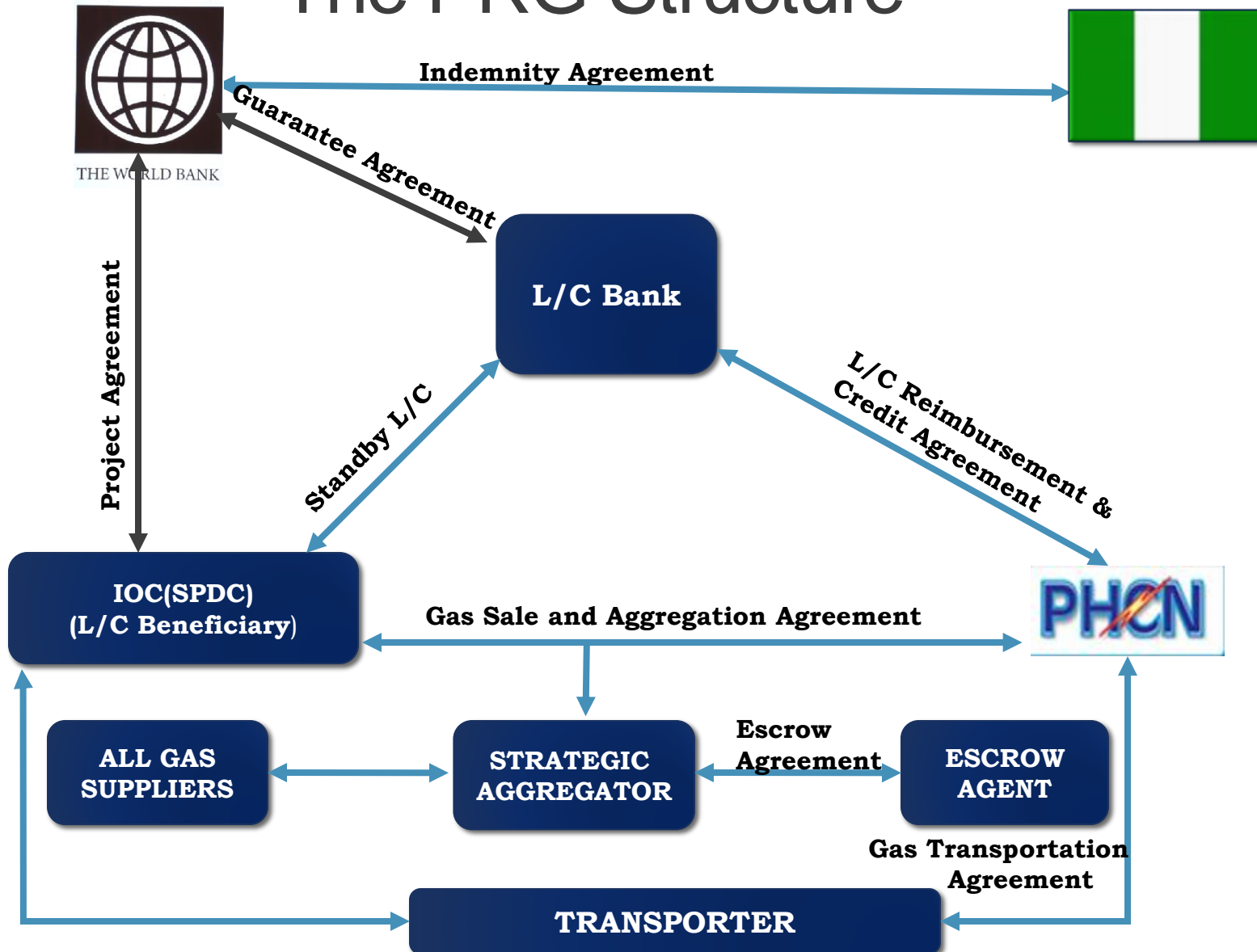
# Payment Security

- **CREDIT RISK a significant issue in gas sale transactions**
- Presently, most gas offtakers are in the power sector & are:
  - 100% owned by FGN
  - Have weak operational structures and financial bases
  - Have an inefficient revenue system
- Risk Mitigation:
  - World Bank's Partial Risk Guarantee (PRG) Instrument
  - Escrow Account
  - Letter of Credit
  - Disputed Amount Account

# THE PARTIAL RISK GUARANTEE

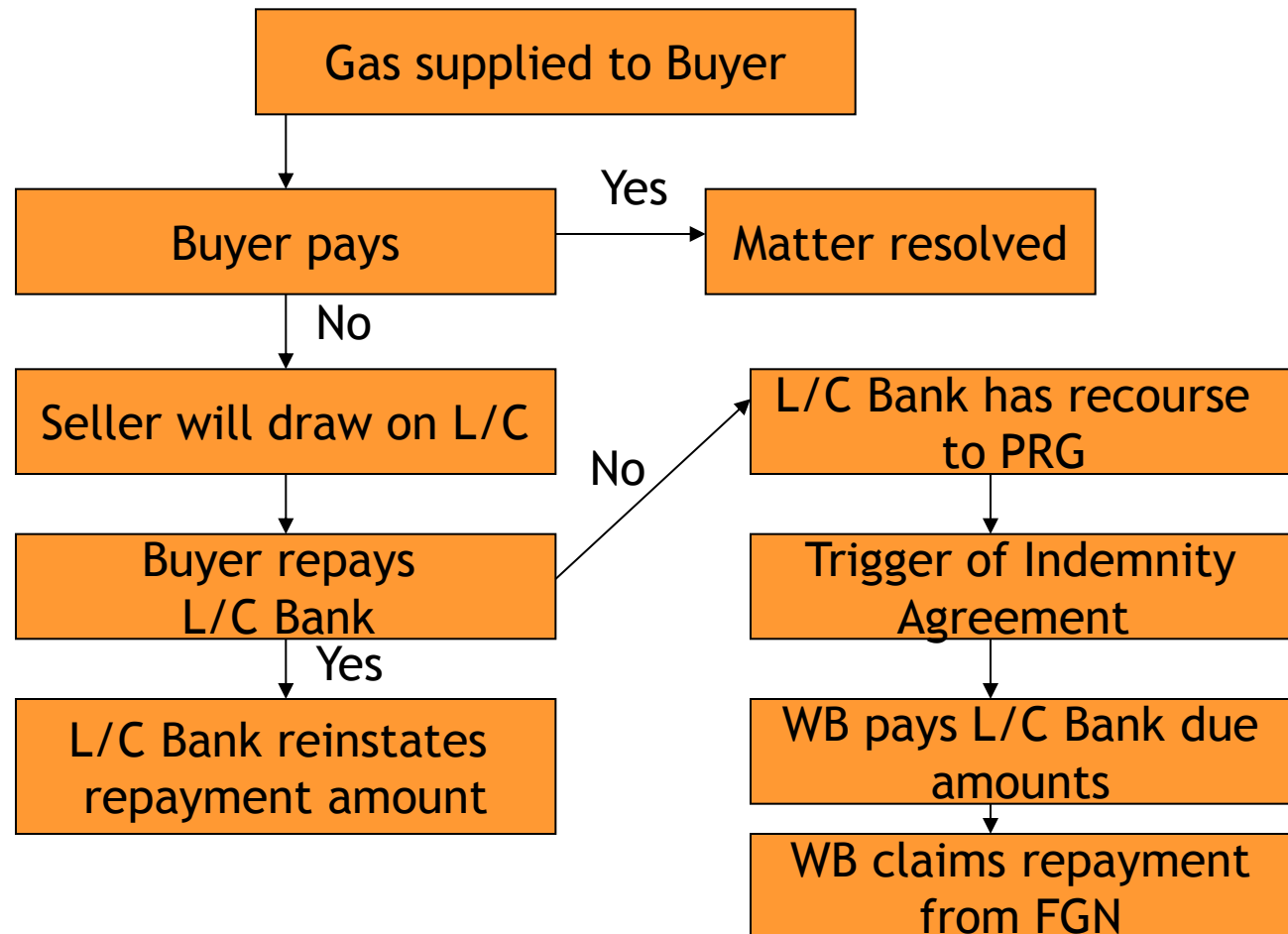
- World Bank instrument
- Intended to back-stop the payment obligations of Buyer under proposed GSAs with Seller
- Will guarantee performance of payment obligations of Government entity
- Letter of Credit (L/C) structure can be utilized to support direct government payment obligations

# The PRG Structure





# How does the PRG work?



# THE ESCROW ACCOUNT

## Rationale:

- To create a pool for the payment of the aggregate price

## Key Features:

- Interest-bearing account for:
  - Receipt, safekeeping and co-mingling of gas purchase consideration from all Buyers; and
  - Disbursement of aggregate price to Sellers based on an aggregate price formula
- Account name – Aggregator's
- Agent – Nigerian bank

# Escrow Account

Implications for the banking & finance sector:

- Huge Transaction - Escrow Agent will manage funds of over US\$bns including:
  - payments by Buyers under their GSAAs;
  - interest income earned on monies in the account; and
  - payments in connection with guarantees such as the PRG by Buyers.
- Retention of Funds/Investment Purpose
  - Upon resignation, Escrow Agent will retain physical custody and control of the Escrow Funds until the Aggregator appoints a successor and notifies the Sellers

# Letter of Credit (L/C)

## Rationale:

- To support Buyer's "take or pay" obligations for gas delivered in accordance with specifications to the 'Delivery Point' and any additional payments for gas nominated by the Buyer

## Key Features:

- To be issued by a Nigerian-based commercial bank
- Issuer must have an international long-term foreign currency grade rating by one of Standard & Poor's or Moody's Investors Services
- Issuer must be acceptable to the Buyer, Seller and World Bank

# L/C

## Process:

- L/C Bank will issue a standby L/C in favour of the Seller at the Buyer's request
- Seller is to draw amounts under the L/C for payments due to it from the Buyer under the GSAA
- Buyer is to reinstate the L/C with amounts drawn under by the Seller

# L/C

## Implications for the banking & financial sector:

- Multiple transactions
  - Each GSAA will be supported by a separate L/C facility
- Increased Liquidity
  - L/C for each GSAA is for a maximum amount equivalent to 10% of the contract value
- Long term Forecast
  - 10 yr L/C term – to match the term of the GSAA's

# L/C

Implications for the banking & finance sector:

- Risk free transaction
  - L/C facility is guaranteed by World Bank (Guarantee Agreement)
- Income Generation
  - Fees will be paid by credit worthy Sellers

# Disputed Amount Account

## Rationale:

- To receive and manage disputed amounts pending determination and settlement

## Key Feature:

- To be maintained with a local commercial bank acceptable to the Buyer, Seller and Aggregator



# Termination

- Events:
  - 10<sup>th</sup> anniversary of the Start Date;
  - Delivery of Contract Quantity
  - Issuance of Termination Notice
  - Failure to maintain financial instrument/Guarantee
  - Re-sale of Gas for unapproved use
  - Operation of Law
  - Expiry/Termination of Sellers' Representative Agreement
- Insolvency
- Prolonged Failure to Deliver Gas
- Prolonged Force Majeure

**TO RECAP: where do the banks come in?**

# OPPORTUNITIES FOR BANKS

- **Potential roles:**
  - LC Bank
  - Escrow Agent
  - Lender for/participant in the financing/development of several projects
- Potential benefits
  - Escrow Fees
  - L/C fees
  - Potential COT revenues

ULTIMATELY, something for everyone.....

Gas  
Producer

Transmission  
Company

Offtaker

The  
Government

The People

Lawyers  
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