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Tax Alert

Federal Government of Nigeria Issues the Upstream Petroleum Operations (Cost Efficiency Incentives) Order,2025

Introduction

In line with the Federal Government of Nigeria's (FGN) commitment to optimizing the management of its petroleum resources and driving efficiency in upstream operations, the FGN, through an official gazette, has issued the Upstream Petroleum Operations (Cost Efficiency Incentives) Order, 2025 (the Order).

The Order, signed by President Bola Ahmed Tinubu, GCFR, aims to address the persistent issue of high operating costs in the upstream oil and gas sector by introducing a structured incentive regime. Prior to now, operating cost in the Nigerian Oil industry has been significantly higher than comparable oil provinces around the world. This initiative aims to realign Nigeria's upstream petroleum operations with global cost benchmarks, eliminate the cost premium, boost competitiveness, and reward efficiency through tax credits.

Here are the key highlights and commentary on the Upstream Operations (Cost Efficiency Incentives) Order,2025.

Highlights

1. Objective and application

The primary objective of the Order is to establish a cost efficiency incentives (CEI) framework that promotes cost discipline and operational efficiency across Nigeria's upstream petroleum sector, thereby increasing Nigeria's competitiveness in the global oil and gas sector.

The order aligns with the provisions of the petroleum Industry Act section 8 which empowers the Nigeria Upstream Regulatory Commission (NUPRC or the Commission) to develop cost benchmarks for the evaluation of upstream petroleum operations. The incentives will apply to all companies operating in the upstream petroleum sector as, Lessees, Licenses and Production sharing Contractors. Lessees, Licenses and Contractors are as defined in the Petroleum Industry Act 2021 (PIA).

2. Cost Efficiency Incentive Benchmark

The Commission, in consultation with industry stakeholders is tasked, on an annual basis, with conducting annual benchmarking studies to establish:

a. Unit Operating Cost (UOC) targets for onshore, shallow water and deep offshore terrains.

b. Cost reduction targets customized to each operator's terrain and production characteristics.

c. Annual assessments within the tax return cycle to evaluate performance against targets.

The Commission will forward the list of qualified companies eligible for the CEI to the Federal Inland Revenue Service (FIRS) and this will serve as a guide to validate taxpayers' claim to the incentives.

3. Tax credit Incentives

Lessees, Licenses and Contractors, whose actual cost in a financial year are below the set cost reduction targets are entitled to tax credits based on a share of the incremental government take saved through cost efficiency.

These tax credits will be applied against the overall tax liability of the Lessees', Licenses', or Contractors' relevant asset, designed to reward companies for cost reductions without compromising existing government revenue expectations. It is important to note that these incentives are **non-transferrable beyond 31 May 2035**. Unless extended or renewed by the President, any unutilized tax credits by this expiration date will become invalid.

4. Calculation and framework of CEI

The formula for computing the CEI is as follows:

CEI = (TOC-AOC) * V * RTR * 50%

Where:

CS is Cost Savings = (TOC – AOC)
RTR is Referenced Tax Rate
AOC is Actual Operating Costs
TOC is Target Operating Cost
V is Annual Fiscal sales of Hydrocarbons
50% is the maximum allowable proportion of CEI from cost savings

It is important to note that CS must be a positive integer to qualify for the incentive. The tax credits must be linked to legitimate, sustainable efficiencies and not derived from unfair practices or prejudicial dealings.

5. Effective Date

The Order took effect on 30 April 2025, with implementation guidelines expected within 30 days, and benchmarking matrices to be published within 90 days of the start of each calendar year. This incentive scheme remains in force until 31 May 2035, unless extended.

Conclusion

The FGN's initiative to promote cost discipline and operational efficiency in upstream petroleum operations is a commendable step toward reshaping the country's oil and gas landscape. By directly linking tax incentives to cost efficiency performance, this policy signals a clear commitment to fiscal responsibility, competitiveness, and economic optimization.

The provisions of the order also balance the incentives with the tax revenue need of the government, by restricting the applicable tax rate for computing the incentives to 30%, regardless of the actual regime of the operator, limiting the lessee/licensee take to 50% of the after-tax savings, and making actual claim each year subject to a maximum of 20% of actual tax liability for the year. Unutilised incentives can be carried forward for three years.

The introduction of the CEI framework can also be viewed as a strategic response to long-standing cost premium challenges in the sector, including prolonged contracting cycles, local content issues and high operating expenses.

As the next phase unfolds, it is expected that the NUPRC and the FIRS will engage the stakeholders and issue comprehensive implementation guidelines. Industry participants are encouraged to begin reviewing their cost structures and aligning internal practices to position themselves for eligibility under this new incentive regime.

If you require further clarification or seek to understand how this would impact your business, please reach out to ngtaxpartners@deloitte.com

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