

NEWSLETTER

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UNLOCKING NIGERIA'S GAS MARKET POTENTIAL: EXAMINING THE GAS TRADING AND SETTLEMENT REGULATIONS, 2023

INTRODUCTION

Since the declaration of the Decade of Gas by the federal government in December of 2020, its disposition towards the development of Nigeria's abundant gas resources has been catapulted significantly. The passage of the Petroleum Industry Act in August of the following year was further reflective of its drive to harness the economic potential of the gas sector. Hardly a few years after, its efforts in developing a robust gas market have taken significant turns with the development of key regulations governing various aspects of the rather enormous market. This is the bedrock upon which the Gas Trading and Settlement Regulations,

2023 were developed and issued by the Nigerian Midstream and Downstream Petroleum Regulatory Authority ("Authority").

The regulations prescribe the requirements for the establishment and operation of gas trading and settlement exchange platforms. By establishing principles for secure, reliable and efficient trading and settlement of natural gas and other gas commodities, the regulations seek to promote and sustain efficient and robust gas trading, exchange and settlement of natural gas and other gas commodities.

ESTABLISHMENT OF TRADING PLATFORMS

The regulations stipulate that any entity aspiring to create a gas trading platform must initiate the process by submitting a comprehensive application to the Authority. This application is expected to contain extensive details, including the proposed platform's business model, governance structure, technical infrastructure, risk management strategies, financial plans, and compliance mechanisms. Moreover, the applicant should demonstrate their capability to meet the necessary financial and operational requirements, including having a minimum paid-up capital as determined by the Authority. This rigorous application process is designed to ensure that only qualified and well-prepared entities are authorized to operate gas trading platforms in Nigeria.

Upon receipt of an application, the Authority shall assess it thoroughly, considering factors such as the applicant's financial standing, technical competence, and adherence to regulatory norms. If the application is deemed satisfactory, the Authority will grant the necessary approval and issue a gas trading license to the applicant. This license authorizes the platform to engage in gas trading activities and obliges it to comply with the regulations, market codes, and rules set forth by the Authority.

FINANCIAL REQUIREMENTS

These regulations outline financial compliance obligations for gas exchanges and clearing houses. They mandate relevant entities to adhere to general financial

requirements specified by the Authority in addition to those of the Securities and Exchange Commission (SEC) for their operation. The Authority retains the discretion to periodically review and modify these requirements to align with risk profiles and other relevant factors. Gas exchanges and clearing houses are further obligated to submit their audited financial statements annually by April 30th for the preceding financial year. Additionally, authorized clearing houses must provide a certificate from their auditors or company secretary, certifying their shareholding pattern and compliance with the regulations during the previous financial year by the same deadline.

The regulations also outline specific financial requirements for gas exchanges operating in Nigeria. Gas exchanges are mandated to establish and maintain a Settlement Guarantee Fund, which serves as a crucial financial instrument to ensure the settlement of trades conducted on the exchange. This fund is initially required to have a minimum balance of USD 500,000, comprising the base minimum capital contributed by all members and any additional balance provided by the gas exchange or clearing house. The regulations also specify that the gas exchange must make quarterly contributions to the Settlement Guarantee Fund, equal to 5% of the total gross revenue generated by the gas exchange or clearing house.

In addition to these contributions, the Settlement Guarantee Fund may also receive returns or income from investments, including the base minimum capital, as well as penalties charged by the gas exchange or clearing house. To ensure the safety of these funds, the

regulations dictate that they must be invested in secure, liquid investments or money market instruments with maturities of less than one year, minimizing exposure to financial risks. The gas exchange is responsible for retaining and managing this fund, and if the clearing function is separated into a distinct clearing house, the fund must be transferred to the clearing house. This ensures that the Settlement Guarantee Fund remains available to cover settlement obligations and defaults, maintaining the financial stability of the gas exchange and the broader gas trading market. Overall, these financial requirements are designed to bolster the financial resilience of gas exchanges and protect market participants in the event of defaults or settlement issues.

MARKET PARTICIPANTS

Market participants include gas producers, gas marketers, gas aggregators, gas shippers, gas suppliers, gas distributors, gas transporters, gas trading licensees, gas clearing houses, and any other entity directly involved in the gas trading value chain. These participants collectively contribute to the development, operation, and maintenance of a dynamic and transparent gas market in Nigeria. The regulations ensure that each market participant adheres to specific rules, responsibilities, and obligations, with the overarching goal of fostering a competitive, secure, and efficient gas trading environment that ultimately benefits the Nigerian energy landscape and its consumers.

RISK MANAGEMENT

The regulations also require gas exchanges and clearing houses to establish prudent and

adaptable risk management processes that align with the evolving risk landscape of their markets. Members are obliged to follow sound risk management policies, including the timely collection of margins from their clients. While the exact amount of margins collected is at the discretion of members, it should, at a minimum, comply with the gas exchange's bye-laws.

Furthermore, gas exchanges must maintain sufficient funds to cover potential liabilities, including pending arbitration cases, arbitration awards, contingent claims, and unresolved grievances of members, trading licensees, or their clients. The Authority is reposed with powers to instruct a gas exchange or clearing house to develop a comprehensive risk management framework, encompassing various aspects such as participant credibility checks, margin requirements for different contracts, adequacy of the Settlement Guarantee Fund, and risks associated with the settlement cycle, among other operational considerations. These measures ensure the integrity and stability of the gas trading market by proactively managing and mitigating risks.

MARKET SURVEILLANCE AND OVERSIGHT

The regulations provide a comprehensive framework to safeguard the gas trading market against fraud, market manipulation, and unethical practices. First and foremost, they mandate the establishment of an Oversight Committee within gas exchanges, responsible for regulatory functions and ensuring market integrity. This committee oversees compliance with the regulations and establishes procedures and reporting formats for disclosure. Additionally, market participants are obligated

to maintain accurate records of transactions, and the regulations empower the Authority to conduct inspections, inquiries, and audits to monitor market activities closely. These inspections can uncover any manipulative activities, anti-competitive behavior, misleading transactions, or price distortions.

Furthermore, the regulations emphasize transparency and equal access. Market participants must provide price-sensitive information on their websites, ensuring the public and other participants can access relevant data. The Surveillance Department of gas exchanges are to monitor daily transactions, analyze bidding patterns, and report any unusual or suspicious activities. This includes tracking dominant participants, sudden spikes in transaction volumes, and defaults. In case of non-public, price-sensitive information that could affect gas trading, the regulations stipulate that individuals must not transact unless such information has been shared with gas facility operators or the gas exchange, thereby reducing the potential for insider trading. Lastly, the regulations establish mechanisms for reporting unscrupulous activities confidentially, providing protection to whistleblowers and empowering the Authority to take strict action against retaliation. Collectively, these measures work to maintain the integrity of the gas trading market and protect it from fraud and manipulation.

CONCLUSION

Essentially, these Regulations represent a significant step towards fostering a transparent, competitive, and secure gas trading environment in Nigeria. They outline comprehensive guidelines for the establishment, operation, and oversight of gas trading platforms, emphasizing fairness, accessibility,

and integrity in the gas market. They define the roles and responsibilities of market participants, promote risk management best practices, and empower the Authority to monitor and intervene if necessary, ensuring market stability and protecting the interests of all stakeholders. By setting forth these comprehensive rules and safeguards, these regulations pave the way for a flourishing gas trading landscape in Nigeria, attracting investments, enhancing energy security, and ultimately driving economic growth in the nation.

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